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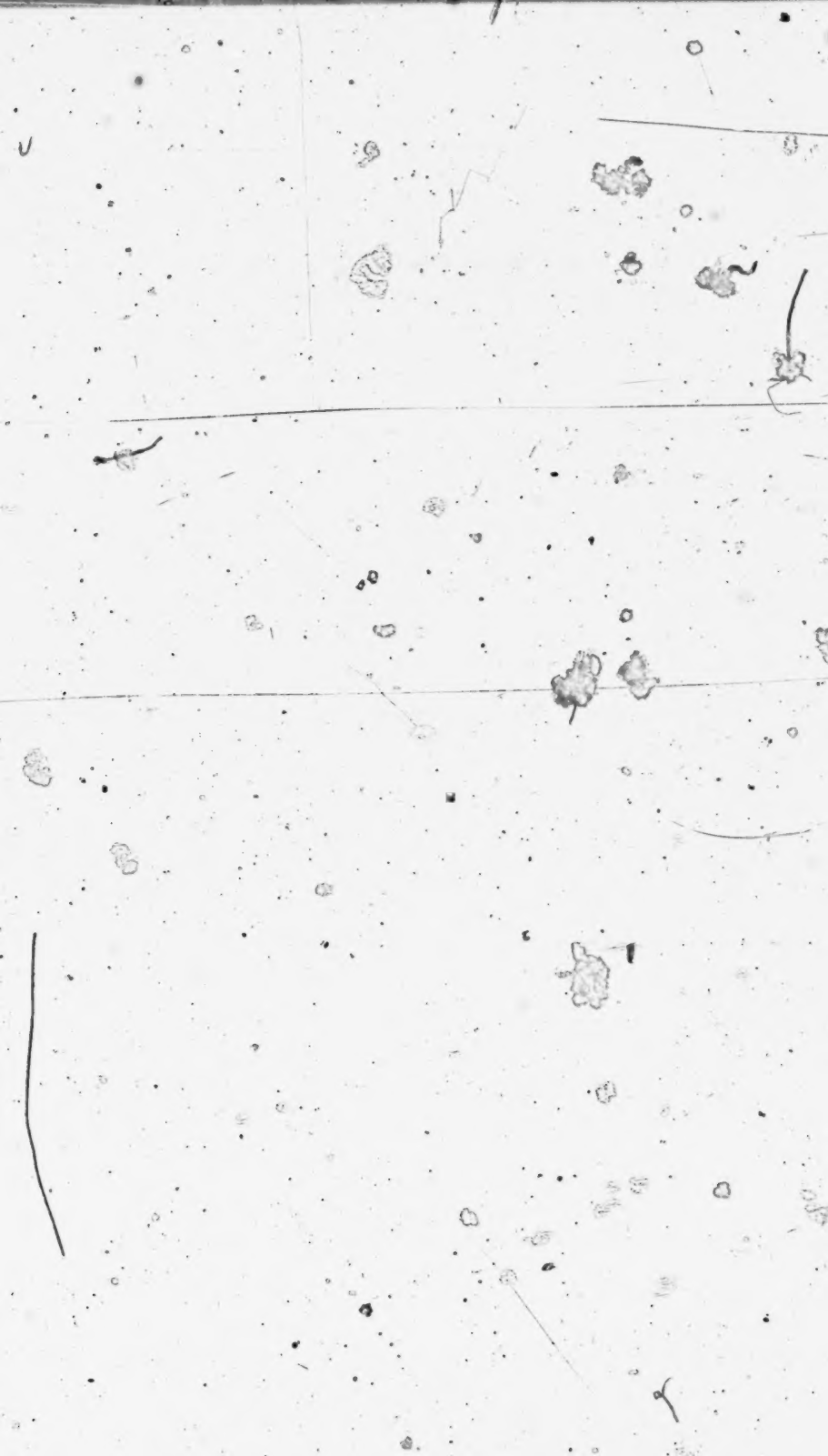
759-329—64——1



1 In the United States District Court for the Northern District of Oklahoma

Pleas and proceedings before the Honorable Luther Bohanon, Judge of the United States District Courts for the Eastern, Western and Northern Districts of Oklahoma, presiding in the following entitled cause:

ATLAS LIFE INSURANCE COMPANY, PLAINTIFF

vs.

UNITED STATES OF AMERICA, DEFENDANT

No. 5413, Civil

Complaint—Filed May 28, 1962

I. Plaintiff presents its Complaint against the United States pursuant to Title 28, Section 1346(a)(1) of the United States Code and Section 7422 of the Internal Revenue Code of 1954.

II. Plaintiff is, and at all times pertinent herein has been, a domestic stock life insurance company incorporated and existing under the laws of the State of Oklahoma, and is a life insurance company as defined in Section 801(a) of the Internal Revenue Code of 1954. Its principal office and place of business is located at 415 South Boston Avenue, Tulsa, Oklahoma.

III. Plaintiff's claim and this suit is for the recovery of $22,782.35, together with interest as provided by law, or such greater amount as is by law refundable, which amount was illegally and erroneously assessed and collected from Plaintiff for the calendar year 1958.

IV. Plaintiff completed and executed and timely filed its Federal Income Tax return for the calendar year 1958 on September 14, 1959, with the District Director of Internal Revenue for the District of Oklahoma.

V. The amount of income tax liability shown due on such return, $64,055.79, was paid by the Plaintiff to the Dis-
2 trict Director of Internal Revenue for the District of Oklahoma by payment of $50,000.00 on March 13, 1959, and payment of $14,055.79 on September 14, 1959.

On August 22, 1961, Plaintiff filed at the office of the District Director of Internal Revenue for the District of Oklahoma its claim for refund of its 1958 tax, claiming refund of such taxes illegally and erroneously assessed and collected from it in the amount of $22,782.35, or such greater amount as was by law refundable. A copy of the claim for refund is hereto attached, marked Exhibit "A," and made a part hereof.

VII. Defendant has taken no final action with respect to the claim for refund for the calendar year 1958 and more than six months have elapsed since Plaintiff filed its claim for refund. This action is filed within the period prescribed by Section 6532(a) of the Internal Revenue Code of 1954.

VIII. Exhibit 1 of the claim for refund, Exhibit A hereto, states the Federal income tax liability for Plaintiff for the calendar year 1958, after giving effect to minor adjustments and corrections, but before making the adjustments as required by Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954, and as required by law.

IX. Plaintiff states that in determining its income tax liability for the calendar year 1958, the Defendant has failed, neglected and refused to make the adjustments required by Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954 and a tax is thus imposed upon all or a part of interest accrued in 1958 from state or local bond obligations owned by Plaintiff, which interest is excluded from gross income under Section 103 of the Internal Revenue Code of 1954.

X. Plaintiff further states that in determining its income tax liability for the calendar year 1958, the Defendant has failed, neglected and refused to make the adjustments under Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954 and thus a tax has resulted on all or part of the interest accrued to Plaintiff in 1958 from state and local obligations, in violation of the principles set forth in National Life Insurance Company v. United States, 277 U.S. 313, (1928) and State of Missouri ex rel Missouri Insurance Company v. Gehner, 281 U.S. 313 (1930), which resulting tax is contrary to the Constitution and laws of the United States.

3 Wherefore, Plaintiff prays judgment against the Defendant in the amount of $22,782.35, or such greater amount as may be due, together with interest as provided by

law, and for its costs, and for such further and other relief to which plaintiff may be entitled.

DICKSON M. SAUNDERS,
of Doerner, Stuart, Moreland, Campbell & Saunders,
BYRON V. BOONE,
of Boone & Ellison,
THOMAS C. THOMPSON, Jr.,
of Bird and Thompson,
Attorneys for Plaintiff.

Exhibit A to Complaint

U.S. Treasury Department—Internal Revenue Service—Claim to be filed with the District Director where assessment was made or tax paid

The District Director will indicate in the block below the kind of claim filed, and fill in, where required.

[ ] Refund of Taxes illegally, Erroneously, or Excessively Collected.
[ ] Refund of Amount Paid for Stamps Unused, or Used in Error or Excess.
[ ] Abatement of Tax Assessed (not applicable to estate, gift, or income taxes).

Please Type or Print Plainly

Name of taxpayer or purchaser of stamps: Atlas Life Insurance Company
Number and street: 415 South Boston
City, town, postal zone, State: Tulsa 3, Oklahoma

Fill in applicable items.

1. District in which return (if any) was filed: Oklahoma City, Oklahoma
2. Name and address shown on return, if different from above:—
3. Period—if for tax reported on annual basis, prepare separate form for each taxable year: From 1–1, 1958, to 12–31, 1958
4. Kind of tax: Corporate Income Tax
4 5. Amount of assessment: $64,055.79; Date of Payment: 3–13–59—$50,000.00, 9–14–59—$14,055.79
6. Date stamps were purchased from the Government:

7. Amount to be refunded: $22,782.35 plus interest legally refundable.

8. Amount to be abated (not applicable to income, estate, or gift taxes):

9. The claimant believes that this claim should be allowed for the following reasons:

See statement and exhibits attached hereto which are made a part of this claim.

The Claimant further claims such additional refund or other relief to which it may be entitled, pursuant to the applicable provisions of the Internal Revenue Code and the regulations thereunder.

I declare under the penalties of perjury that this claim (including any accompanying schedules and statements) has been examined by me and to the best of my knowledge and belief is true and correct.

Signed ATLAS LIFE INSURANCE COMPANY,
By: HARRY L. SEAY, Jr., *President*.

Dated August 22, 1961.

Attachment to Exhibit A

[Copy]

Statement
Atlas Life Insurance Company
Claim for Refund—1958 Federal Income Taxes

Taxpayer hereby claims that it erroneously overpaid its 1958 income tax by the amount of $22,782.35. The amount of tax previously assessed and collected from claimant for 1958 was erroneous and illegal to the extent it resulted in an overpayment of tax for such year. Claimant overpaid its 1958 tax because no adjustments were made as required by Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code in computing its "life insurance company taxable income" to prevent imposition of tax on state and municipal bond interest accrued during the year, which is excluded from gross income under Section 103 of the Code. When the adjustments required by Sections 804(a)(6) and 809(b)(4) are made to eliminate the imposition of tax on state and municipal bond interest accrued by claimant in 1958, a lesser tax liability for 1958 results and refund of the excess taxes erroneously paid is hereby claimed.

5 Unless the proper adjustments are made, "the application of the definition of taxable investment income" (as defined in Section 804(a)(2)) and "the application of the definition of gain from operations" (as defined in Section 809(a)(1)) impose a tax on part or all of the state and municipal bond interest accrued by claimant in 1958 ($36,637.79).

Before the proper adjustments for tax exempt interest can be made three minor technical corrections are necessary. These corrections result in a lesser tax liability for 1958 and refund of the overpayment of 1958 taxes on account of the correction of these errors is also claimed. Attached hereto as Exhibit 1 is a revised 1958 tax return correcting these errors and omissions. Exhibit 1 does not take into account the adjustments provided in Sections 804(a)(6) and 809(b)(4). In detail Exhibit 1 makes the following corrections to claimant's 1958 tax return as filed:

(1) On its 1958 tax return as filed, claimant did not deduct 2% of its group accident and health insurance premiums as provided for in Section 809(d)(6) and Regulations Section 1.809–6. Under Exhibit 1, a deduction of 2% of claimant's group accident and health insurance premiums in the amount of $24,257.43 has been taken, increasing the deduction under Section 809(d)(6) from $23,492.31 to $47,749.74 (Schedule E, Line 25(a)).

(2) On its 1958 tax return as filed, claimant computed its investment income on the cash basis rather than on the accrual basis as required by Section 818(a) and Regulations Section 1.818–2. Exhibit 1 corrects this error by computing investment income on the accrual basis. This results in increasing the amount of state and municipal bond interest from $36,202.79 to $36,637.79 (Schedule A, Line 1(a), Column 4), decreasing the amount of interest from United States obligations issued after March 1, 1941, from $47,453.34 to $44,540.34 (Schedule A, Line 1(d), Column 4), and decreasing the amounts received from loans, notes, mortgages, etc., from $885,768.49 to $885,515.37 (Schedule A, Line 1(e), Column 4). These corrections result in an overall decrease in gross investment income from $969,424.62 to $966,693.50 (Schedule A, Line 1, Column 4).

(3) On its 1958 tax return as filed, claimant eliminated from assets due and unpaid premiums and reinsurance premiums due from other companies for 1958 and the

preceding four years in computing the adjusted reserves rate under Section 805(b). Regulations Section 1.805–5(a)(4) provides for the inclusion of such items in assets when computing the adjusted reserves rate. Exhibit 1 includes these amounts in assets in determining the adjusted reserves rate. This inclusion decreases the adjusted reserves rate from 3.32573% reported on claimant's 1958 tax return as filed, to 3.25846% (Schedule B, Part III, Line 7) in Exhibit 1.

Exhibit 1, as a result of correcting the above-described omissions and errors, shows that claimant's 1958 tax liability is $58,128.84, before making the adjustments provided in Sections 804(a)(6) and 809(b)(4).

Attached hereto are Exhibits 2 and 3 which are alternative computations of claimant's 1958 tax liability. These computations give effect to the adjustments provided for in Sections 804(a)(6) and 809(b)(4). When these computations are compared with that in Exhibit 1, they establish that the application of the definition of "taxable investment income" (Sections 804(a)(2)) and of the definition of "gain from operations" (Section 809(b)(1)), without adjustment, result in the imposition of tax on state and municipal bond interest accrued by claimant during 1958.

Exhibit 2 computes claimant's 1958 tax liability (after making the corrections and additions made in Exhibit 1) by excluding all state and municipal bond interests accrued in 1958 and the prior four years from gross investment income (Section 804(b), Schedule A, Line 1(a)). This results in computing claimant's 1958 "life insurance company taxable income" without taking into account any amount of tax exempt interest (as if it had not received any tax exempt interest in 1958 or in the prior four years) all other facts during these years remaining unchanged.

A comparative analysis of the tax computations under Exhibits 1 and 2 is attached. The comparison of the two exhibits shows that the direct result of excluding tax exempt interest from all items of the tax computation in Exhibit 2 is to reduce "taxable investment income" by $10,992.61 ($83,936.17 minus $72,943.56) and to reduce "gain from operations" by $32,928.36 ($160,790.13 minus $127,861.77). This results in Exhibit 2 showing a reduction in "life insurance company taxable income" of $21,960.49

($122,363.15 minus $100,402.66) which in turn reduces claimant's tax liability for 1958 from $58,128.84 in Exhibit 1 to $46,709.38 in Exhibit 2 by an amount of $11,419.46.

7 The attached comparison of Exhibits 1 and 2 demonstrates that the inclusion of tax exempt interest in the formulas which compute the percentage of net investment income, i.e., investment yield, included in the insurance company's income base under Sections 804(a)(2) (defining "taxable investment income") and 809(b)(1) (defining "gain from operations") directly increases the amount of investment yield included in income. Thus, the company's share of investment yield included in "taxable investment income" is decreased from 12.9312% in Exhibit 1 to 11.6263% in Exhibit 2 as a result of excluding all tax exempt interest. (See further Items 7 and 8 of comparative analysis.) Also, the attached comparison demonstrates that the exclusion of tax exempt interest in Exhibit 2 in computing "gain from operations" directly results in decreasing the company's share of investment yield from 10.1246% in Exhibit 1 to 6.2158% in Exhibit 2. (See further Items 14 and 15 of comparative analysis.)

Exhibit 3 computes claimant's 1958 tax liability by including the full amount of tax exempt interest in gross investment income as is done in Exhibit 1. Exhibit 3, Schedule C, deducts (rather than excludes) the policy and other contract liability requirements (Line 4, Schedule B, Part 1) from the investment yield (Line 14, Schedule A) to obtain the amount of investment yield included in taxable investment income. The resulting figure ($113,673.88) is the same as in Exhibit 1. Similarly, Exhibit 3, Schedule E, deducts (rather than excludes) the required interest (Line 5, Schedule E–1) from the investment yield (Line 4, Schedule A) to obtain the amount of investment yield included in gain from operations. Again, the resulting figure ($89,001.87) is the same as in Exhibit 1. Further, in Exhibit 3, the full amount of tax exempt interest accrued in 1958 is deducted; in Exhibit 1, only the company's share of tax exempt interest is deducted.

A comparative analysis of the tax computations under Exhibits 1 and 3 is attached. This comparison of Exhibits 1 and 3 shows that the effect of the adjustments in the tax computation in Exhibit 3 is to reduce "taxable investment income" by $31,900.08 ($83,936.17 minus $52,036.09) and to reduce "gain from operations" by $32,928.36 ($160,790.13 minus

$127,861.77). The amount of reduction in "taxable investment income" and "gain from operations" is exactly the amount of the difference between the deductions of tax exempt interest in Exhibit 1 (which deducts only the so-called company's share of tax exempt interest) and Exhibit 3 (which deducts all tax exempt interest). See further Items 11 and 18 of comparative analysis.

8 The attached comparison of Exhibits 1 and 3 further shows that the adjustments made to the "application of the definition of taxable investment income" and to the "application of the definition of gain from operations" in Exhibit 3 reduces 1958 "life insurance company taxable income" by $32,414.22 ($122,363.15 minus $89,948.93) which decreases claimant's 1958 tax liability by $16,855.40 ($58,128.84 minus $41,273.44).

Claimant reserves the right to submit further computations and to offer proof under Sections 804(a)(6) and 809(b)(4) to establish additionally that the application of the definition of "taxable investment income" in Section 804(a)(2) and of the definition of "gain from operations" in Section 809(b)(1) without adjustment results in the imposition of tax on state and municipal bond interests accrued in 1958. For example, the deduction allowed in Schedule E, Exhibit 1, for increase in reserves is directly contrary to the tax exemption concept laid down by the United States Supreme Court in National Life Insurance Company vs. United States, 277 U.S. 313, (1928). This results because Exhibit 1 requires that the deduction be reduced by the entire amount of the tax exempt interest excluded (i.e. the so-called policy holders' share). Specifically:

Total increase in reserves	$1,480,610.37
Minus "policyholders' share" (Line 8, Schedule E), includes policyholders' share of tax exempt interest	790,064.38
Amount of deduction for increase in reserves allowed	$690,545.99

To be in accord with the National Life decision, the calculation should deduct only the policyholders' share of "other items of investment yield." Specifically:

Total increase in reserves	$1,480,610.37
Minus "policyholders' share" (Line 7, Schedule E), does not include policyholders' share of tax exempt interest	757,136.02
Amount of deduction for increase in reserves allowed	$723,474.35

The resulting "gain from operations" is the same as in Exhibits 2 and 3. This demonstrates that the calculation of "gain from operations" as required by Exhibit 1 erroneously overstates the policyholders' "gain from operations" by $32,928.36, the amount of the so-called policyholders' share of tax exempt interest.

9 Moreover, as a further alternative claim, claimant contends that the computation of "life insurance company taxable income" for 1958 without adjustment results in imposing a tax on the state and municipal bond interest accrued by claimant during the year and is, therefore, in conflict with the constitutional principles affirmed by National Life Insurance Company vs. United States, 277 U.S. 313 (1928) and Missouri vs. Gehner, 281 U.S. 313 (1930). Therefore, in any event, an adjustment to the computation of claimant's 1958 "life insurance company taxable income" is necessary to prevent the imposition of an unconstitutional federal income tax.

[Three copies of exhibits 1 to 3, computations and alternative computations, and the comparative analysis of exhibits 1 and 2 and exhibits 1 and 3 have been filed.]

In United States District Court for the Northern District of Oklahoma

Amendment to Complaint—Filed June 29, 1962

Comes now the Plaintiff, and within the time prescribed by the Federal Rules of Civil Procedure, and amends its Complaint heretofore filed on May 28, 1962, by the inclusion therein and addition thereto of the following paragraph, designated as Paragraph XI, to-wit:

XI. Plaintiff further states that in determining the income tax liability of the Plaintiff for the calendar year 1958, the Defendant has imposed a tax upon all or part of interest accrued to Plaintiff in 1958 from state and local bond obligations, and that the Defendant, in the determination and application of said tax, has thereby imposed a tax on Plaintiff contrary to the Constitution and the laws of the United States.

Wherefore, Plaintiff prays judgment against the Defendant in the amount of $22,782.35, or such greater amount as may be due, together with interest as provided by law, and for its

costs, and for such further and other relief to which Plaintiff may be entitled.

DICKSON M. SAUNDERS,
of Doerner, Stuart, Moreland, Campbell & Saunders,
BYRON V. BOONE,
of Boone & Ellison,
THOMAS C. THOMPSON, Jr.,
of Bird and Thompson,
Attorneys for Plaintiff.

Filed June 29, 1962.

In United States District Court for the Northern District of Oklahoma

Answer—Filed July 26, 1962

10 The defendant, United States of America, by its attorney, John M. Imel, United States Attorney for the Northern District of Oklahoma, for its answer to the Complaint herein alleges as follows:

I. Admits the allegations contained in paragraph I of the Complaint.

II. Admits the allegations contained in paragraph II of the Complaint.

III. Admits the allegations contained in paragraph III of the Complaint, except denies that any amount of income taxes was illegally and erroneously assessed and collected from the plaintiff for the calendar year 1958.

IV. Admits the allegations contained in paragraph IV of the Complaint.

V. Admits the allegations contained in paragraph V of the Complaint, except alleges that the amounts stated therein were paid by the plaintiff on March 16, 1959 and September 15, 1959, respectively.

VI. Denies the allegations contained in paragraph VI of the Complaint, except admits that Exhibit A of the Complaint is a true copy of the claim for refund filed by the plaintiff on August 22, 1961, but denies all allegations set forth in the said claim for refund which are not otherwise admitted herein.

VII. Admits the allegations contained in paragraph VII of the Complaint.

VIII. Alleges that it is presently without knowledge or information sufficient to form a belief as to the truth of the

allegations contained in paragraph VIII of the Complaint, except denies that any adjustment to the plaintiff's federal income tax liability is required by the provision of Sections 804(a)(6) and 809(b)(4) of the Int rnal Revenue Code of 1954.

IX. Denies the allegations contained in paragraph IX of the Complaint.

X. Denies the allegations contained in paragraph X of the Complaint.

11 XI. Denies the allegations contained in paragraph XI of the Amended Complaint.

Wherefore, defendant prays that the Complaint and the Amended Complaint be dismissed with prejudice and that the defendant have its costs and disbursements.

UNITED STATES ATTORNEY.
By: L. K. SMITH,
Assistant U.S. Attorney.

In United States District Court for the Northern District of Oklahoma

Pre-Trial Order—Entered December 10, 1962

A pre-trial conference was held in the above cause on November 21, 1962, Dickson M. Saunders, Byron V. Boone and Thomas C. Thompson, Jr. appeared as counsel for the Plaintiff, and Sam E. Taylor, Assistant United States Attorney, Tulsa, Oklahoma, and George Hrdlicka, Department of Justice, Washington, D.C., appeared as counsel for the Defendant.

This is an action for the recovery of $22,782.35, together with interest as provided by law, or such greater amount as is by law refundable, brought by Plaintiff in connection with its claim for Federal income taxes that the Plaintiff alleges were erroneously and illegally assessed and collected for the year 1958 under the Life Insurance Company Income Tax Act of 1959.

Plaintiff contends that:

1. The application of the definition of taxable investment income (Sec. 804(a)(2) of the Internal Revenue Code of 1954) and the application of the definition of gain from operations (Sec. 809(b)(1) of the Internal Revenue Code of 1954) results in the imposition of a tax on all or a part of interest accrued in 1958 from state or local bond obligations owned by Plaintiff, which interest is excluded from gross income under Sec. 103 of the Internal Revenue Code of 1954, for:

(a) in determining its income tax liability for the calendar year, 1958, the Defendant has failed, neglected and refused to make the adjustments required by Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954 and a tax is thus imposed upon all or a part of interest accrued in 1958 from state or local bond obligations owned by Plaintiff, which interest is excluded from gross income under Section 103 of the Internal Revenue Code of 1954; and for

(b) in determining its income tax liability for the calendar year 1958, the Defendant has failed, neglected and refused to make the adjustments under Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954 and thus a tax has resulted on all or part of the interest accrued to Plaintiff in 1958 from state and local obligations, in violation of the principles set forth in National Life Insurance Company v. United States, 277 U.S. 313, (1928) and State of Missouri ex rel Missouri Insurance Company v. Gehner, 281 U.S. 313 (1930), which resulting tax is contrary to the Constitution and laws of the United States.

2. In determining the income tax liability of the Plaintiff for the calendar year 1958, the Defendant has imposed a tax upon all or part of interest accrued to Plaintiff in 1958 from state and local bond obligations, and that the Defendant, in the determination and application of said tax, has thereby imposed a tax on Plaintiff contrary to the Constitution and the laws of the United States.

Plaintiff claims that its evidence will establish:

1. That the application of the definition of taxable investment income (Sec. 804(a)(2) of the Internal Revenue Code of 1954) and the application of the definition of gain from operations (Sec. 809(b)(1) of the Internal Revenue Code of 1954) to Plaintiff result in the imposition of a tax on its interest from state and local bond obligations in that:

(a) The Life Insurance Income Tax Act of 1959, and the Treasury Regulations thereunder, adopt formulas dividing the investment yield of the Plaintiff between the policyholders and the Company, and because such formulas take into account exempt interest from the state and local bond obligations, the exclusions from Plaintiff's non-exempt income are automatically reduced.

(b) The exclusion of the policyholders' share of tax exempt interest does not prevent the imposition of a tax upon all

or a part of Plaintiff's interest from state and local bond obligations.

13 (c) The deduction of the Company's share of tax exempt interest does not prevent the imposition of a tax upon all or a part of Plaintiff's interest from state and local bond obligations.

(d) Solely because of the receipt or accrual of interest from state and local bond obligations the tax on Plaintiff's non-exempt income is automatically increased.

(e) The Defendant has failed to make or to permit adjustments as provided by Sec. 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954.

2. The reserve requirements are liabilities of Plaintiff and are essential parts of the computation of Plaintiff's tax.

The Defendant contends that:

1. A tax has not been imposed on income from state and local bond obligations.

2. The Life Insurance Income Tax Act of 1959, and the Treasury Regulations thereunder, adopted formulas allocating the investment yield of the Company between policyholders and the Company, and that such formulas properly may take into account interest from state and local bond obligations without imposing a tax on such interest.

3. The investment yield set aside for policyholders (reserve requirements) is not subject to any income tax because it is excluded from the Plaintiff's taxable investment income.

4. All income from state and local bond obligations allocated to the Company is fully deducted and, therefore, not taxed.

5. The Life Insurance Company Income Tax Act of 1959 is constitutional as applied by the Defendant to Plaintiff.

The following questions of law are involved:

1. Does the application of Plaintiff of the definition of taxable investment income (Sec. 804(a)(2) of the Internal Revenue Code of 1954) and the application to Plaintiff of the definition of gain from operations (Sec. 809(b)(1) of the Internal Revenue Code of 1954) impose a tax on its exempt interest from state and local bond obligations so as to require adjustment to be made as provided in Sec. 804(a)(6) and Sec. 809(b)(4) of the Internal Revenue Code of 1954 to prevent the imposition of such a tax?

14 2. Does the Life Insurance Company Income Tax Act of 1959 impose a greater tax on the Plaintiff's income from non-exempt sources solely because of the receipt or ac-

crual of exempt interest from state or local bond obligations, and, if so, was it within the constitutional power of Congress to impose such a tax?

Orders of the Court

1. The Annual Reports of Atlas Life Insurance Company for the years 1954, 1955, 1956, 1957 and 1958, as filed with the Insurance Department of the State of Oklahoma, may be offered and received in evidence without further identification.

2. The 1958 Federal income tax return of Plaintiff may be offered and received in evidence.

3. The 1958 Federal income tax return of Plaintiff, based upon the revised figures from the Revenue Agent's Report of September 4, 1962, as computed without application of Sections 804(a)(6) and 809(b)(4) of the Internal Revenue Code of 1954, subject to verification by Defendant of the correctness of the mechanical application of mathematics and arithmetic to such return based on the Revenue Agent's Report, may be offered and received in evidence. This revised 1958 tax return shows the agreed tax liability of the Plaintiff for that year except as may be modified by this Court's decision on the issues in this cause.

4. The bonds, assets, and all items of property set forth in the Annual Reports referred to in paragraph numbered 1 above will be considered as assets owned by Plaintiff, unless Defendant after examination by its agents thereof has proof to the contrary.

Witnesses and Exhibits of the Parties

1. Plaintiff will offer the following witnesses for oral testimony:

(a) Johnson D. Hill, Jr., Executive Vice President, Atlas Life Insurance Company, 415 South Boston, Tulsa, Oklahoma.

(b) Andrew Delaney, Senior Vice President, American General Life Insurance Company, Houston, Texas.

(c) A member of the staff of the office of Joe B. Hunt, Insurance Commissioner of the State of Oklahoma.

2. Plaintiff will offer the following exhibits:

(a) Items number 1, 2 and 3 of Orders of the Court.

(b) Additional tax computations and reconciliations for income received or accrued during the year 1958 in support of Plaintiff's contentions.

2. Defendant will furnish the names of its witnesses and the list of its exhibits within a reasonable time following the taking of depositions by Defendant of the three witnesses enumerated above on the part of Plaintiff.

Depositions

Plaintiff will have available the three witnesses enumerated above at 1218 Atlas Life Building, 415 South Boston Avenue, Tulsa, Oklahoma, on December 5, 1962 at 9:30 A.M. for the purposes of depositions.

Entered this 10th day of December, 1962.

LUTHER BOHANON, *Judge.*

Approved as to form:

DICKSON M. SAUNDERS,
Attorney for Plaintiff.
GEORGE HRDLICKA,
Attorney for Defendant.

Filed Dec. 12, 1962.

In United States District Court for the Northern District of Oklahoma

Before LUTHER BOHANON, United States District Judge.

Opinion—May 1, 1963

This case involves a claim for income tax refund for the year 1958. Atlas Life Insurance Company, a corporation, hereinafter referred to as Atlas or Taxpayer, filed this suit against the United States of America seeking a refund in the sum of $22,782.35, or such greater amount as may be due, for alleged over-assessment by the Government of income taxes for the year 1958. The claim for refund has been reduced to $12,692.93, not by the pleadings, but by the evidence offered on behalf of Atlas and by Atlas' final Brief filed with the Court.

Plaintiff filed its tax return for the year 1958 in due time and thereafter timely filed its claim for refund. No action having been taken by the Government within the time provided by law, 26 U.S.C.A. 7422(a), thereafter this action was filed, as required by 26 U.S.C.A. 6532(a).

Certain adjustments in the Atlas' return show it entitled to a refund of $1440.74. This amount is not in dispute.

759-329—64——2

The claim made here by Atlas involves the application and interpretation of the Internal Revenue Code of 1954, as amended by the Life Insurance Company Income Tax Act of 1959, 26 U.S.C.A. 801 et seq.

Atlas contends that by the application of the definition of "Taxable Investment Income" (Section 804(a)(2)) and of the application of the definition of "Gain From Operations" (Section 809(b)(1)) of the Act results in the imposition of a tax on tax-free interest from state and municipal bonds owned by Atlas, which interest income should be excluded from its gross income under Section 103 of the Internal Revenue Code of 1954, 26 U.S.C.A. 103; Atlas claims that the Government refused to make adjustments required by Sections 804(a)(6) and 809(b)(4), thus imposing a tax on tax-exempt interest which is excluded from gross income under Section 103, supra.

By the Internal Revenue Code of 1954, as amended by the Life Insurance Company Act of 1959, hereinafter called the Act, Congress provided a method of taxing life insurance companies, taking into consideration interest which is not to be included in gross income under Section 103. This interest is one of several factors to be employed in determining the amount of the Taxpayer's taxable income. We are here concerned only with two phases of the various steps involved in arriving at taxable income; that is, (1) taxable investment income, and (2) gain from operations.

Considering the first, "taxable investment income": The Act, Section 804(a) (1) and (2) provides:

17 (a) In general.—

(1) Exclusion of policyholders' share of investment yield.—The policyholders' share of each and every item of investment yield (including tax-exempt interest, partially tax-exempt interest, and dividends received) of any life insurance company shall not be included in taxable investment income. For purposes of the preceding sentence, the policyholders' share of any item shall be that percentage obtained by dividing the policy and other contract liability requirements by the investment yield; except that if the policy and other contract liability requirements exceed the investment yield, then the policyholders' share of any item shall be 100 percent.

(2) Taxable investment income defined.—For purposes of this part, the taxable investment income for any taxable year shall be an amount (not less than zero) equal to the amount

(if any) by which the net long-term capital gain exceeds the net short-term capital loss plus the sum of the life insurance company's share of each and every item of investment yield (including tax-exempt interest, partially tax-exempt interest, and dividends received), reduced by—

(A) the sum of—

(i) the life insurance company's share of interest which under section 103 is excluded from gross income.

(ii) the deduction for partially tax-exempt interest provided by section 242 (as modified by paragraph (3)), computed with respect to the life insurance company's share of such interest, * * *

Section 804(a)(6) provides:

Exception.—If it is established in any case that the application of the definition of taxable investment income contained in paragraph (2) results in the imposition of tax on—

(A) any interest which under section 103 is excluded from gross income,

(B) any amount of interest which under section 242 (as modified by paragraph (3)) is allowable as a deduction, * * * adjustment shall be made to the extent necessary to prevent such imposition.

18 The pertinent section of the Act relating to gains from operations, Section 809(b), provides:

(b) Gain and loss from operations.—

(1) Gain from operations defined.—For purposes of this part, the term "gain from operations" means the amount by which the sum of the following exceeds the deductions provided by subsection (d):

(A) the life insurance company's share of each and every item of investment yield (including tax-exempt interest, partially tax-exempt interest, and dividends received);

(B) the amount (if any) by which the net long-term capital gain exceeds the net short-term capital loss; and

(C) the sum of the items referred to in subsection (c).

(2) Loss from operations defined.—For purposes of this part, the term "loss from operations" means the amount by which the sum of the deductions provided by subsection (d) exceeds the sum of—

(A) the life insurance company's share of each and every item of investment yield (including tax-exempt interest, partially tax-exempt interest, and dividends received);

(B) the amount (if any) by which the net long-term capital gain exceeds the net short-term capital loss; and

(C) the sum of the items referred to in subsection (c).

(3) Life Insurance company's share.—For purposes of this subpart, the life insurance company's share of any item shall be that percentage which, when added to the percentage obtained under the second sentence of subsection (a)(1), equals 100 percent.

Section 809(b)(4) provides:

(4) Exception.—If it is established in any case that the application of the definition of gain from operations contained in paragraph (1) results in the imposition of tax on—

(A) any interest which under section 103 is excluded from gross income.

(B) any amount of interest which under section 242 (as modified by section 804(a)(3) is allowable as a deduction, * * * adjustment shall be made to the extent necessary to prevent such imposition.

There is no dispute about the facts. A question of law only is presented here which can be resolved by an examination of the testimony, briefs, and especially the Taxpayer's return and the definition of "taxable investment income" and "gains from operations" as defined by the Act, supra.

Determination of taxable investment income and gain from operations is determined as follows: Taxable investment income: from gross investment income, Section 804(b), which includes tax-exempt interest, less certain deductions, Section 804(c)(1), resulting in a figure known as "investment yield," Section 804(c). This yield is then divided into two parts, (1) the policyholders' share, (2) the company's share. This division is made by the use of a percentage determined as provided by Section 805 of the Act. The entire part belonging to the policyholders as determined by the formula, including tax-exempt interest, is excluded from taxable income, Section 804(a)(1). The company's portion of each item of investment yield is then reduced by its portion of tax-exempt interest and other specified deductions, Section 804(a)(2). The resulting figure is the company's tax base for "taxable investment income," the first phase upon which the tax is imposed. Tax-exempt interest on the company's share of investment income, as can be seen, is wholly excluded in arriving at the final figure representing taxable investment income.

Turning to the second phase, gain from operations: Entering into the Taxpayer's taxable income is included the company's share of each item of investment yield, including tax-exempt interest, long-term capital gain, and other items includible in gross income under Section 61, Internal Revenue Code of 1954 (26 U.S.C. 958 edition, Section 61) not otherwise included: Sections 809(b)(1) and 809(c). This amount is reduced by certain deductions, including the company's share of tax-exempt interest (809(d)(8)). Tax-exempt interest with respect to gain from operations is treated exactly in the same manner as such interest is treated in determining taxable investment income. The problem involved here is the application of the formula for treatment of tax-exempt interest with respect to taxable investment income and gain from operations. By use of the formula provided by Section 804(a)(2) and Section 809(b)(1) the percentage of the policyholders' share of income in this case is less than it would be if tax-exempt interest was not included or considered in gross income for the purpose of the computation as provided by Section 804, supra, thereby leaving a greater portion as the company's share, resulting in a greater tax liability.

Atlas' Exhibit 6, being its return filed in compliance with the Act and regulations of the Internal Revenue Service, shows the policyholders' share of investment income is 85.33% plus, and the company's share 14.66% plus, and the policyholders' share of gain from operations 87.93% plus, and the company's share 12.66% plus. Atlas' Exhibit 7, being a tax form prepared by it in line with its theory of the law, excludes from any consideration all tax-exempt interest, and shows the policyholders' share of investment income as 86.64% plus, and the company's share 13.39% plus, and gain from operations 91.12% plus and 8.87% plus, respectively, reducing the amount of the company's income and thus its tax. The Taxpayer contends that under Section 804(a)(6) and 809(b)(4), the exception provisions of the Act, the application of the formula used by the Government results in a tax on its non-taxable interest income and therefore an adjustment should be made to prevent such tax. Under the formula used by the Government and as provided by the Act, company's tax-exempt interest is included in gross income and then deducted before reaching the tax base of the Taxpayer. The Taxpayer's formula excludes tax-exempt interest from the beginning. The inclusion or exclusion of tax-

exempt interest results in the difference between the tax imposed and the claimed refund.

Atlas contends that the formula for determining its income tax is unconstitutional in that a tax is laid upon its tax-exempt interest income. I do not agree. The Act simply classifies income for purposes of taxation and no tax is laid upon tax-exempt interest received by Atlas. The Power of Congress to lay and collect taxes is plenary subject only to certain constitutional restrictions not here present. The Congress may classify incomes for the purpose of taxation. The formula provided by Congress is for all similar life insurance companies and does not discriminate against any, including Atlas.

21 To adopt the formula urged by Atlas would amount to a striking down of the formula adopted by Congress, which this Court will not approve, and at the same time set up a formula not provided by Congress. In the Atlas formula it gives no consideration to interest from tax-exempt securities as income. This is certainly unrealistic. For the power of Congress to classify income and lay a tax thereon see Denman vs. Slayton, 282 U.S. 514. In this case the Taxpayer was engaged in buying and selling tax-exempt municipal bonds. In 1922 he collected $65,720.06 as interest on these securities and paid out $78,153.84 for interest on money borrowed in due course to purchase and carry exempt securities. In his tax return he excluded the interest so collected and claimed a deduction for interest paid out on borrowed money. The Tax Commissioner disallowed the deduction. The Court said:

"Determination of the question involved must turn upon the validity, construction and effect of Sections 213 and 214, Revenue Act of 1921, 42 Stat. 227, 237, 238, 239. Their pertinent provisions follow.

'Sec. 213. That for the purposes of this title * * * the term "gross income"— * * *

'(b) Does not include the following items, which shall be exempt from taxation under this title: * * *

'(4) Interest upon (a) the obligations of a State, Territory, or any political subdivision thereof, or the District of Columbia; * * *

'Sec. 214. (a) That in computing net income there shall be allowed as deductions: * * *

'(2) All interest paid or accrued within the taxable year on indebtedness, except on indebtedness incurred or continued

to purchase or carry obligations or securities (other than obligations of the United States issued after September 24, 1917, and originally subscribed for by the taxpayer) the interest upon which is wholly exempt from taxation under this title; * * *' "

The taxpayer in Denman vs. Slayton, supra, contended that the exception found in paragraph (2), Section 214(a) conflicts with the Federal constitution in that by necessary operation it discriminates against owners of non-taxable securities; also that the Act is discriminatory and unconstitutional in
22 that necessary expenses incident to all kinds of businesses, including interest paid for carrying inventories, et cetera, are allowed as operation costs, whereas deduction of interest paid by the taxpayer upon funds borrowed to carry non-taxable securities is prohibited. Taxpayer further contended that the Act is arbitrary and unconstitutional for it discriminates against him whose resources do not permit him to purchase tax-free securities for cash. The Court then said, Page 519:

"While guaranteed exemptions must be strictly observed, this obligation is not inconsistent with reasonable classification designed to subject all to the payment of their just share of a burden fairly imposed. * * * The classification complained of is not arbitrary, makes no improper discrimination, does not result in defeating any guaranteed exemption, and was within the power of Congress. The fact that respondent engaged in the business of buying and selling is not important."

The exception provisions of the Act, 804(a)(6) and 809 (b)(4) were enacted by Congress to make doubly sure that tax-exempt interest would not in fact be taxed and that if by some misapplication of the formula or mathematical error it is taxed, then by application of these provisions an adjustment would be made.

Atlas relies heavily on National Life Insurance Company vs. United States, 277 U.S. 508, and State of Missouri, ex rel Missouri Insurance Company vs. Gehner, 281 U.S. 313. These cases do not support the Taxpayer's position. In National Life the Court held as unconstitutional Section 245(a) of the Revenue Act of 1921, 42 Stat. 227, which provided that a reserve deduction allowed to all insurance companies should be reduced by the amount of tax-exempt interest received. The Court in essence held that by pro tanto denying a deduction solely by reason of receipt of tax-exempt interest, the

Congress had imposed a tax on that interest which was constitutionally exempt. In Missouri vs. Gehner, the Court held unconstitutional a state property tax on net worth of insurance companies which, in computing net worth, allowed a deduction for federal bonds, but required a pro rata deduction in the deduction that was otherwise allowable for insurance reserves. No comparable denial of deductions is made by the Act here in question. These cases cannot be so narrowly construed as urged by Atlas. See Denman vs. Slayton, supra.

Having reached the conclusion that by the application of the Act, tax-exempt interest received by Atlas is not in fact taxed, judgment will be entered denying the claimed refund, except to the extent of $1,440.74 resulting from adjustments agreed upon by the parties.

Dated this 1 day of May, 1963.

LUTHER BOHANON,
United States District Judge.

23 In United States District Court for the Northern District of Oklahoma

Judgment—May 1, 1963

Based upon the Opinion of the Court filed this date,

It Is Ordered, Adjudged And Decreed by the Court that plaintiff's claim for refund in the sum of $1,440.74, with interest, should be allowed.

It Is Further Ordered that the remaining claim for refund of the plaintiff should be denied.

Judgment Is Entered Accordingly.

Dated this 1st day of May, 1963.

LUTHER BOHANON,
United States District Judge.

In United States District Court for the Northern District of Oklahoma

Notice of Appeal—Filed June 21, 1963

Notice is hereby given that Atlas Life Insurance Company, a corporation, Appellant herein, hereby appeals to the United States Court of Appeals for the Tenth Circuit from the Judgment entered in this action by the United States District Court for the Northern District of Oklahoma on the 1st day of May,

1963, insofar as said Judgment denies the remaining claim for refund of Plaintiff therein, Appellant herein designated, over and above the sum allowed to Plaintiff in the amount of $1,440.74, with interest, and the United States of America is hereby designated Appellee.

DICKSON M. SAUNDERS,
of Doerner, Stuart, Moreland, Campbell & Saunders,
BYRON V. BOONE,
of Boone & Ellison,
THOMAS C. THOMPSON, Jr.,
of Bird and Thompson,
Attorneys for Appellant.

24 [An appeal bond was filed June 21, 1963.]

In United States District Court for the Northern District of Oklahoma

Statement of Points—Filed July 9, 1963

The points upon which Appellant intends to rely in this Appeal are as follows:

1. The Trial Court erred in failing to determine that Plaintiff had overpaid its Federal Income Taxes for the year 1958 in the amount of $12,692.93, and to grant a refund thereof.

2. The Trial Court erred in failing to determine the question of fact and of law that Defendant's application of the Life Insurance Company Income Tax Act of 1959 to Plaintiff in respect of the year 1958 resulted in the imposition of Federal Income Tax on interest on state and other local governmental obligations, which interest is excluded from gross income under Section 103 of the Internal Revenue Code.

3. The Trial Court erred in failing to determine the question of fact and of law that Defendant's application of the definition of "'taxable investment income" in Section 804(a)(2) of the Internal Revenue Code and "gains from operations" in Section 809(b)(1) of the Internal Revenue Code to Plaintiff in respect of the year 1958 resulted in the imposition of Federal Income Tax on interest excluded from gross income under Section 103 of the Internal Revenue Code.

4. The Trial Court erred in failing to determine that it was necessary pursuant to the provisions of Section 804(a)(6) and

Section 809(b)(4) of the Internal Revenue Code to adjust Defendant's determination of Plaintiff's income tax liability for the year 1958 to prevent the imposition of Federal Income Tax on interest excluded from gross income under Section 103 of the Internal Revenue Code.

5. The Trial Court erred in failing to determine that Defendant's application of the Life Insurance Company Income Tax Act of 1959 to Plaintiff in respect of the year 1958 was contrary to the intent of Congress in enacting such Act and violated the Constitution of the United States.

Dated this 9th day of July, 1963.

DICKSON M. SAUNDERS,
of Doerner, Stuart, Moreland, Campbell & Saunders,
BYRON V. BOONE,
of Boone & Ellison,
THOMAS C. THOMPSON, Jr.,
of Bird and Thompson,
Attorneys for Appellant.

25 [By order of July 24, 1963, the time for docketing the cause in the Court of Appeals was extended to August 15, 1963.]

In United States District Court for the Northern District of Oklahoma

Excerpts From Transcript of Trial Proceedings
Tulsa, Oklahoma, December 27, 1962

Appearances: For the Plaintiff: Doerner, Stuart, Moreland, Campbell & Saunders, (by) Dickson M. Saunders, Boone & Ellison, (by) Byron Boone, Bird & Thompson. For the Defendant: George Hrdlicka, Department of Justice, Washington, D.C., Sam E. Taylor, Assistant United States Attorney, Northern District of Oklahoma.

The COURT. The case on the trial docket this morning is Atlas Life Insurance Company vs. United States of America. Is the plaintiff ready?

Mr. SAUNDERS. Plaintiff is ready, your Honor.

The COURT. Defendant ready?

Mr. HRDLICKA. Defendant is ready, your Honor.

The COURT. Very well. The rest of the docket will be called later in the day.

Mr. BOONE. If the Court please, in this case I believe Government counsel at the pretrial mentioned something about the importance of the case to the Government. It is just equally as important to the taxpayers of the country; and we have with us this morning a representative of the City of Tulsa and also a Mr. Zarra who represents the New York Port Authority. They would like to sit in this case and with your Honor's permission file an amicus curiae brief later, and with your permission I think they would like to make a short statement along with ours when the case starts or proceeds, if that is satisfactory with your Honor.

The COURT. Very satisfactory indeed. The parties are indeed welcome to this court. Thank you, Mr. Boone.

26 JOHNSON D. HILL, JR., called as a witness on behalf of the plaintiff, being of lawful age and having first been duly sworn, testified as follows:

Direct Examination by Mr. SAUNDERS:

Q. State your name. A. Johnson D. Hill, Jr.

Q. Where do you live, Mr. Hill? A. Tulsa, Oklahoma.

Q. What is your occupation?

A. I am Executive Vice President and Assistant Treasurer of the Atlas Life Insurance Company.

Q. That's the plaintiff in this case? A. That's correct.

Q. How long have you held that position? A. Six years.

Q. What are your duties with the plaintiff as Executive Vice President and Assistant Treasurer?

A. My duties are of a general supervisory nature over the operations of the company. In the absence of senior officers I function in their stead.

Q. Do you have any duties with relation to Atlas insofar as investments are concerned?

A. I participate in the management decisions with respect to investments, yes.

Q. Are you a member of the Investment Committee? A. I am.

Q. Could you please tell us, Mr. Hill, the policies and procedures followed by the Atlas Life Insurance Company in making investments?

A. Atlas Life invests in farm and urban residential first mortgage loans and in securities.

We invest with respect to securities largely in bonds. We look for as high a yield as we can obtain commensurate with the quality of the bond. The term of the bond and the maturity have a bearing also.

Q. When you speak of seeking a yield, a high yield commensurate with the other safety factors, do you and the other members of the Investment Committee give consideration to federal income taxes?

A. We do. We are concerned primarily with a yield after federal taxes.

Q. Are the investments of Atlas Life Insurance Company regulated by Oklahoma law? A. No, they are not. There are some restrictions in the Oklahoma law with respect to the proportion of certain types of investments to total assets. Other states have similar restrictions but as far as regulation, there is no state regulation.

Q. Mr. Hill, do you know what are life insurance reserves?

A. Yes. Life insurance—you mean reserves on life insurance contracts?

27 Q. Yes, sir.

A. Reserves are calculations of the future liabilities under outstanding policy contracts. The methods by which those reserves are calculated are primarily in the realm of our Actuarial Department. Generally they involve the use of mortality tables, certain interest assumptions, and valuation methods.

* * * * * *

The COURT. What are all of them? Let's just admit them all at one time. What are the exhibits?

Mr. SAUNDERS. Exhibit No. 1 is the annual statement of Atlas Life Insurance Company for the year 1958; Exhibit No. 2 is the annual statement for the company for 1957; Exhibit No. 3 is the annual statement for the year 1956; Exhibit No. 4 is the annual statement for 1955; Exhibit No. 5 is the annual statement for 1954; Exhibit No. 6 is computation of the 1958 income tax liability for Atlas Life Insurance Company, reflecting the adjusted figures as a result of the Revenue Agent's report. It's not the original return. It has been agreed upon with counsel for the defendant that this copy may be introduced.

28 Exhibits 7 through 16 thereafter, your Honor, are alternate tax computations based on the particular tax

return for 1958. Exhibit No. 7 as being the subsidiary to Exhibit No. 6 is likewise the 1958 tax return of Atlas Life Insurance Company, adjusted however to exclude all items of tax exempt income.

* * * * *

Exhibit 9 is a computation based on the 1958 tax return showing, however, the effect of an increase of $1000 of additional income within the category of wholly taxable investment income.

Exhibit 10 likewise is based on the 1958 tax return but to show the receipt of an additional $1000 of tax exempt income for interest from state and local bond obligations.

* * * * *

29–30 Q. (By Mr. SAUNDERS.) Does Atlas Life Insurance Company, and in particular you on the Investment Committee, take into account these life insurance reserves you spoke of a moment ago in making company investments? A. No, we do not.

Q. Do the reserves for life insurance contracts you mentioned a moment ago have any relation to your current investments or investment returns? A. No.

Q. Who makes the computations of the reserves, Mr. Hill?

A. Our Actuarial Department.

Q. Is there any requirement that the Actuarial Department make its computations pursuant to any state law?

A. The state has laws as to minimum reserve requirements and our procedures are in conformity with that, those regulations and laws.

Q. If there is no relationship between your investments and your reserves, what is the purpose of establishing the life insurance contract reserves?

A. The purpose of the reserves is to in a sense guarantee the non-forfeiture of values in the contract and to assure that the future liabilities under our various outstanding contracts will be met.

Q. Are the reserves assets of the company?

A. They are not. They are liabilities of the company.

Q. When you make an investment on behalf of Atlas Life Insurance Company, do you earmark that investment for any particular purpose? A. No.

Q. Are the increases and decreases in reserves reflected on the books of Atlas Life Insurance Company?

A. They are not reflected on the books, Mr. Saunders, if you mean by books ledger accounts and so on. Records are kept, of course, of the reserves and the totals for each class of outstanding contracts is calculated and the aggregate total is calculated once a year, but there are no ledger or journal entries with respect to reserves.

Q. In the actuarial computation of the reserves, is there an assumed rate of interest taken into consideration? A. There is.

Q. Now on the other side of the company management, when making an investment, is this assumed rate of interest taken into consideration? A. No, no, I would say it is not.

Q. Is there any requirement under state law to obtain a certain rate of return on any investment that Atlas makes?

A. Not to my knowledge.

Mr. SAUNDERS. That's all.

31 Cross-Examination By Mr. HRDLICKA:

Q. Mr. Hill, I wanted to clarify one point. You made a statement that state law has no control over your investment policy. That's not entirely true, is it, sir?

A. I believe I qualified that by pointing out that there are restrictions as to the total volume of investments of certain types.

Q. So that the statutes do impose certain restrictions as to the amount of investment in certain types of securities and other general restrictions and limitations, is that true?

A. To an extent, sir.

Q. And your investment policy stays within this statutory requirements, I assume? A. It does.

Q. You mentioned an assumed rate of interest. What is the purpose of the assumed rate of interest?

A. I am not sure I understand your question, sir.

Q. You mentioned in your direct testimony that you have occasions to use or employ an assumed rate of interest as opposed to an actual rate of interest, to your investment earnings, I would assume.

Now what is the purpose of using, how do you use that assumed rate of interest?

A. My reference to interest assumption, sir, was in connection with reserves, not to investments.

Q. To what do you apply the interest assumption?

A. Well, it is part of the formula, along with the valuation method, which is used to calculate the reserves.

Q. So that——

A. (Interposing.) It's in a sense a discount of future premiums.

Q. I see, and the assumed interest then is used to increase reserves, is that correct, or to decrease if that should be appropriate under the formula?

A. I am not sure I follow you there, sir. You are getting into a field that's somewhat technical. I am not an actuary.

Q. Don't you have an assumed interest factor which is applied against certain assets and anticipates future earnings for the purpose of setting premiums; or is that beyond your knowledge, and I will withdraw it.

A. Would you ask the question again? I'm sorry.

Q. Don't you have an assumed interest rate which is applied to certain investment assets to obtain a future investment picture for the purpose of establishing your premiums on policies?

A. I would say no to that question.

Q. I believe you stated that you make no distinction between the type of investment for purposes of reserves, is that correct?

A. That is true.

32 Q. Is there any distinction made on money that you receive from your investments as to how that money should be used or as to where it should be applied? A. No, there is not.

Q. So that all money received by the company is treated exactly the same, is that correct, irrespective of the type of security? A. That is true.

Q. You also mentioned that the reserve is a liability. In what sense is it a liability?

A. It's an obligation of the company.

Q. I mean how is it carried as a liability? On the balance sheet is it carried as a liability?

A. In our statement it is—you are speaking now of policy reserves?

Q. Yes.

A. Policy reserves are included along with other reserves as to liabilities.

Q. What is the purpose for carrying this reserve as a liability in your annual statements and on your balance sheet?

A. What is the purpose of carrying it——?

Q. Why is it carried as a liability?

A. Because it is a liability.

Q. Could you explain this, what does it cover?

A. Well, if I understand your question correctly, it covers among other things the cash and loan values.

Q. What about the exposure to the company on policies issued? Does it have anything to do with that; does it have anything to do with the anticipated exposure to the company on insurance policies issued? A. Yes, it does.

Q. And so it also covers that item, is that correct?

A. That is true.

ANDREW DELANEY, called as a witness on behalf of the plaintiff, being of lawful age and having first been duly sworn, testified as follows:

Direct Examination By Mr. SAUNDERS:

Q. What is your name? A. Andrew Delaney.

Q. Where do you live, Mr. Delaney? A. At Houston, Texas.

Q. What is your occupation? A. Actuary.

Q. Are you a consulting actuary or are you employed on a regular basis? A. No, I am employed by several life insurance companies.

33 Q. Would you name them, please, and your capacities?

A. Yes. I am Senior Vice President and Director of the American General Life Insurance Company at Houston, Texas; Vice President and Actuary of the Knights Life Insurance Company of Wilmington, Delaware; Vice President and Actuary of the Hawaiian Life Insurance Company of Honolulu; Vice President and Actuary and Assistant Secretary of the Home State Life Insurance Company of Oklahoma City.

Q. Are you a member of any professional societies or organizations? A. I am a member, I am a Fellow of the Society of Actuaries.

Q. Are you a member of any industry committees?

A. Yes, I am a member of the Joint Advisory Committee on Interpretation of Company Federal Income Tax Law.

Q. And who makes up the joint committee you speak of?

A. This is a joint committee of the American Life Convention and the Life Insurance Association of America, which are trade organizations the members of which hold 95% of all the assets of life insurance companies.

Q. How long have you been an actuary? A. For sixteen years.

Q. What is your educational background in connection with your actuarial work?

A. I have an A.B. from Oberlin College in Ohio and a B.S. from New York University in New York City.

Q. What has been your business experience?

A. From 1946 to 1949, I served as mathematician with the Equitable Life Insurance Society of the United States, in New York City. From 1949 to 1954, I served as Assistant Actuary of the Union Central Life Insurance Company of Cincinnati, Ohio, and in 1954 I joined the American General.

Q. Now did you serve as actuary for those companies you mentioned? A. I served in the Actuarial Department of those companies.

Q. Can you tell us generally what function an actuary performs?

A. Yes. An actuary bears the principal responsibility for determining a company's premiums, for valuing its liabilities. In the case of a mutual company, for setting its dividends scale. He usually helps draft the policy forms and computes the nonforfeiture value in those policy forms. He advises the company management in connection with compliance with the nonforfeiture laws of the various states and in general he is the company officer to whom management looks for advice about mortality experience, assumed interest rates and lapse rates used in premium calculations.

Q. You mentioned earlier that you were a Fellow of the Society of Actuaries. Are there any requirements for achieving this status?

A. Yes, there are a series of eight examinations which are conducted by the Society of Actuaries, and after completion of the eight examinations, the designation of Fellow is awarded.

34 Q. Are you employed by Atlas Life Insurance Company? A. No.

Q. Have you ever performed any actuarial services for Atlas Life Insurance Company? A. No.

Q. Are you familiar with the books and records of Atlas Life Insurance Company?

A. Yes, I have examined the books and records of the company in its home office in Tulsa.

Q. Are you also familiar with the annual statements filed by Atlas Life Insurance Company in the office of the Oklahoma Insurance Commissioner? A. Yes.

Q. These have been identified as Exhibits 1 through 5 inclusive. Have you examined those? A. Yes.

Q. Do you know, Mr. Delaney, whether or not Atlas Life Insurance Company was audited for federal income tax purposes in 1958?

A. Yes.

Q. Have you examined the Revenue Agent's report on that audit?

A. Yes.

Q. In your capacity for these various companies by whom you have been employed and by whom you are employed at the present time, have you had occasion to prepare federal income tax returns?

A. Yes, I am responsible for the preparation in all of the companies for which I now work.

Q. And for how many years past have you been preparing income tax returns for life insurance companies? A. For about ten years.

Q. Have you prepared a 1958 income tax return for Atlas Life Insurance Company, based on the 1959 Life Insurance Company Income Tax Act? A. Yes.

Q. What materials did you use in the preparation of that?

A. Used the company's books and records, the 1958 annual statement and the annual statement for the four preceding years, and also the adjustments made by, made in the Revenue Agent's report.

Q. Have you made a number of alternate computations of tax based upon the figures reflected in that income tax return in the company books and records, the annual statement and the Revenue Agent's report? A. Yes.

Q. Before we go to these returns you have prepared, Mr. Delaney, can you tell us what are life insurance reserves?

A. Yes. Let me begin by defining the meaning of present value as used by an actuary. If a series of payments is to be made in the future, the value of that series of payments to a recipient is something less than the aggregate sum which you will receive because if you had that sum in hand now, you could earn interest on it and hence it would be worth more to him.

35 Let me illustrate that by saying, if you are to receive $1000 a year each year for ten years, the present value of that—the single sum which if you held it in your hand now would be equivalent to that series of payments—will of course depend upon the interest rate.

For example, at 6% interest, it is $7,360.09. The actuary would then say that $7,360.09 is the present value of that series of payments, discounted for interest. If a series of payments to be made in the future is also going to depend upon whether a particular individual is alive, the actuary would also take into account the probability that that individual might be dead in determining the present value, and he would then say the present value of that series of payments was discounted for interest and mortality.

Let me say that, with that background, that at the time of issue of any life insurance contract, the present value of net premiums contracted to be paid on that policy is exactly equal to the present value of the death benefits provided by the contract. The death benefits are of course the sum insured.

At any time after issue, however, the present value of the future net premiums is somewhat less because there are fewer future net premiums to be paid on the contract. At the same moment, present value of the future death benefits is somewhat greater because the probable date of death has drawn nearer.

The difference between the increased present value of these future death benefits and the decreased present value of the future net premiums constitutes the life insurance reserve.

Q. Is this an asset of the company?

A. No, this is a liability of the company.

Q. Are the reserves on each policy issued, by Atlas for instance, the same?

A. No, the reserves vary for each class of policy and by age at issue.

Q. Do you know how this particular company, Atlas, computes its reserve? A. Yes.

Q. Could you tell us, please?

A. Yes. Atlas has established reserve standards based on assumed interest rates, assumed mortality tables many years ago; and each year at the end of the year they take an inventory of their existing policies and apply to this inventory of policies in force the reserves based on these assumed mortality tables and interest rates, and total the reserves for each class

of policies. The total reserve for the company is the aggregate of the reserve for each class of policy.

36 Q. Did the reserves for Atlas Life Insurance Company increase in 1958? A. Yes.

Q. Why did the reserves increase?

A. The reserve increased because the application of the reserve factors to the year end inventory at December 31, 1958 was more than the application of the reserve factor to the inventory of policies in force at December 31, 1957.

Q. Did the earnings of Atlas Life Insurance Company, either reflected in the annual statement or in the federal income tax returns or in the books and records, have any bearing on the computation of those reserves?

A. None whatsoever. The reserves are based, as I said previously, on assumed interest rates and mortality tables.

Q. In 1958, Mr. Delaney, what would have been the situation if Atlas Life Insurance Company had earned more on its investments than shown on its federal income tax return with reference to its reserves?

A. Reserves would have increased exactly the same amount.

Q. Suppose, Mr. Delaney, for 1958 Atlas had not earned any return on its investments, would the reserves have increased or decreased?

A. They would have increased exactly the same amount because they have no relationship to the actual company earnings.

Q. Are the reserves for Atlas Life Insurance Company reflected by any funds? A. No, they are liabilities of the company.

Q. In your examination of the Atlas books and records in its home office and other data that you examined, have you found any segregation or earmarking of any assets? A. None whatsoever.

Q. Where on the books of Atlas are these reserves that you spoke of reflected?

A. They are not reflected on the company's books.

Q. Mr. Delaney, I hand you what has been marked for purposes of identification as Plaintiff's Exhibit No. 6 and ask you to state what it is.

A. This is the 1958 tax return of the Atlas Life prepared on the basis consistent with the Internal Revenue Service Regulations.

Q. Do you have a copy of that in your possession?

A. Yes, I do have.

Q. In this 1958 tax computation, on this particular form, are there any provisions to determine the application of the so-called exception clauses for tax exempt interest? A. No.

Q. What is the liability shown under that computation for 1958 federal income tax?

A. The liability for 1958 is shown on line 6 of page 1, and is $62,615.05.

37 Mr. SAUNDERS. If your Honor please, just so the record may be fully complete, I believe that Exhibit 6 has been received in evidence through stipulation with Government counsel.

Mr. HRDLICKA. That is correct.

The COURT. That is right.

Q. (By Mr. SAUNDERS). Can you tell us on this 1958 tax return how the amount of taxable investment income was computed?

A. Yes. The first step is to determine the company's investment yield. This is shown in Schedule A on line 14. Schedule A is on page 2 of the tax return. The company's investment yield is determined by including all items of investment income, including interest on state and municipal bonds and subtracting therefrom the investment expenses incurred in earning that investment income, and also subtracting certain other deductions permitted by the law.

Q. Does this return show the investment yield on line 14 in the amount?

A. Yes, the return shows that the investment yield for 1958 for the Atlas Life, on line 14, Schedule A, page 2, was $894,277.61.

Q. What is the next step necessary to be made in computing the company's taxable investment income for 1958?

A. The next step is to determine the policy and other contract liability requirements.

Q. Can you tell us generally what are policyholder and other contract liabilities?

A. Generally speaking, the policy and other contract liability requirements is that part of the increase in reserves assumed to come from interest earnings adjusted for the company's invested yield rate.

Q. Now that you have told us what this is, how do you compute the policyholder and other contract liability requirements?

A. The first step is to determine the company's earnings rate. These are determined by dividing the investment yield by the company assets. The calculation is contained on page 2, Schedule B, Part 3.

The next step is to adjust the company's life insurance reserves for the investment yield rate and this step is calculated on page 3 of the tax return in Schedule B, Part 5.

The next step is to multiply the company's investment yield rate by the adjusted life insurance reserves, and to add to this total the interest actually paid by the company. This step is contained on page 2 of the tax return, Schedule B, Part 1.

38 The total policy and other contract liability requirements is then for the Atlas Life in 1958 shown on page 2, Schedule B, Part 1, line 4, to be $763,144.28.

Q. Now is there a relation between the investment yield that you testified was on line 14 of Schedule A and this policyholder and other contract liability requirements?

A. Yes, the next step in the calculation is to determine the policyholders' share which is shown on page 3 of the return, Schedule C, line 1. This policyholders' share is equal to the policy and other contract liability requirements divided by the investment yield.

Q. What is that percentage?

A. That percentage for Atlas Life in 1958 is 85.33-plus percent, shown again on line 1 of Schedule C.

The next step is to determine the company's share, which is equal to 100 minus the policyholders' share. This is shown on line 2 of Schedule C to be 14.66-plus percent.

Q. Then what is the next step in computing its taxable investment income?

A. The next step in computing taxable investment income is to exclude from the investment yield the policyholders' share. This is done on lines 4, 5, 6 a[illegible] of Schedule C; and you will note by examining the tax return that there has been excluded $31,265.37 of tax exempt interest and $731,878.95 of other items of investment yield.

The resulting figure is shown on line 8, Column 3 of Schedule C, and is $131,133.29.

Q. Is that the tax base upon which the income tax liability is computed?

A. No, from this is deducted the company's share of the tax exempt interest shown on line 9 of Schedule C, and also the

small business deduction, line 12 of Schedule C, so that the taxable investment income is on line 14 of Schedule C, is $100,760.87.

Q. Mr. Delaney, in the literature surrounding the 1959 Life Insurance Company Income Tax Act, the hearings before both houses of Congress and otherwise, is this computation of taxable investment income what is known generally as the "Phase 1 tax"?

A. Yes, it is, and that, the figure on line 14 of Schedule C is carried over to the first page of the tax return and appears again in line 1–a on page 1 of the tax return.

Q. After completing the Phase 1 computation, what is the next step in determining income tax liability?

A. The next step is to calculate the gain from operations and the first step in this calculation is to determine the policyholders' share ratio for Schedule E, which appears on page 3–a of the tax return.

39 Q. Now this gain from operations that you are talking about, is that what is known generally in the literature and the hearings as the Phase 2 tax computation?

A. Yes, it is. That is known as Phase 2, and the gain from operations includes all items of income such as premiums and all other receipts, all items of investment income, and from this he deducted the death benefits, the increase in reserves and so forth.

Generally speaking, in the gain from operations follows page 4 of the company's annual statements, but there are some differences.

Q. What is the next step in connection with determining Phase 2, gain from operations income?

A. The step is to determine the policyholders' share. To do this we must first determine the company's required interest. This is calculated on page 4 of the tax return in Schedule E–1 and is equivalent to multiplying the reserves by the interest rate assumed in those reserves.

The figure for Atlas Life in 1958 appearing on line 5 of Schedule E–1, page 4, is $781,540.32.

Q. Mr. Delaney, is it true to state that this figure of $781,000-plus is computed from tabular tables of interest and assumptions?

A. Yes, the reserves are based on tabular interest assumptions and tabular mortality tables, and the required interest

figures depend only on these assumed interest rates and mortality tables.

Q. Would receipt of tax exemption be reflected in this Schedule E–1 of required interest?

A. No, since it is determined entirely from tabular items, the company's actual investment experience has no relationship to it.

Q. Then what is the next step?

A. Having determined the required interest, we divide the required interest by the investment yield, again from line 14 of Schedule A, and determine the policyholders' share which is shown on line 1 of Schedule E, page 3–a, and for Atlas Life in 1958 it's 87.39-plus percent.

The company's share is equal to 100 minus the policyholders' share, and this is shown on line 2 of Schedule E, and for Atlas Life it was 12.60-plus percent.

Q. Are there any further steps to be taken in computing the gain from operations?

A. Yes, the next step then is to exclude from the investment yield the policyholders' share. This is done on lines 4, 5, 6 and 7, Schedule E, and you will note that excluded in this computation was $32,019.04 of tax exempt interest and $749,521.28 of other items of investment yield.

Q. Then are other items of receipt and deduction taken into consideration in preparing the Phase 2 tax?

A. Yes. Then to the investment, taxable investment yield which appears on line 8 of Schedule E, we add all the company's receipts, premiums and so forth, and subtract from it the death benefits, the increase in reserve—the increase in reserve—excuse me, after reduction for investment yield as shown on line 14 of Schedule E, and we come back to the gain or loss from operations which appears on line 27 of Schedule E, and for the Atlas Life in 1958 it was $161,220.08.

Q. How do you use this figure then to compute the income tax liability for 1958?

A. The figure of $161,220.08 is then carried to line 1–b of page 1, and life insurance company taxable income is then determined to be the amount on line 1–a, which was the taxable investment income, plus 50 percent of the excess of the gain from operations over the taxable investment income. In the case of Atlas Life for 1958, the 50 percent amounted to $30,229.61, so that the total life insurance company taxable income,

which appears on page 1, line 3, was $130,990.48; and to that figure is applied the regular corporate income tax to determine the company's tax liability.

Q. Mr. Delaney, I hand you what has been marked for purposes of identification as Plaintiff's Exhibit No. 7 and ask you to tell us what it is.

A. This is a *calculation* of the 1958 tax return for Atlas Life computed exactly as the 1958 tax return, Exhibit 6, except that we have excluded from this tax return all items of investment yield.

Q. Yield? A. Tax exempt investment, excuse me.

Q. Do you have a copy of that? A. Yes, I do have.

Mr. SAUNDERS. Plaintiff now offers into evidence Plaintiff's Exhibit 7, the testimony by this expert witness.

Mr. HRDLICKA. Defendant objects on the ground that it is argumentative, irrelevant and immaterial.

The COURT. Overruled.

(Plaintiff's Exhibit 7 was received in evidence; see page 12.)

Q. (By Mr. SAUNDERS.) What is the amount of tax liability as shown on page 1 of Plaintiff's Exhibit 7?

A. The total tax liability is shown as $51,362.86.

Q. Did you make any assumptions in preparing this Exhibit 7?

41 A. Yes. As stated earlier, we omitted all the company's tax exempt investment income from our calculations. Thus on page 2, line 14 of Schedule A, the investment yield is in this case shown as $857,639.82, which is equal to the investment yield shown in the company's 1958 tax return less $36,637.79 of tax exempt interest.

Q. Is there a difference in this exhibit 7 and the tax return as filed with respect to the amount of policy and other contract liability requirements?

A. Yes, because of the change in, because of the omission of the tax exempt interest, the policy and other contract liability requirements shown in Schedule B, Part 1 in this exhibit, is $743,137.55 which is less than the policy and other contract liability requirements in the company's 1958 tax return.

Q. Can you explain this difference?

A. The difference occurs because the company's earnings rate are somewhat less in this exhibit, because we are dividing the investment yield, which is less because of the omission of the tax exempt interest, by the same assets and the reduction in

these earnings rates causes the decrease in the policy and other contract liability requirements. The difference in percentage is shown in Exhibit 2, Schedule—pardon me, in Exhibit 7, Schedule C. The liability requirements in this exhibit is divided by the investment yield. The policyholders share as shown on Schedule C, line 1 is 86.64-plus percent which is more than the policyholders' share in the company's 1958 tax return.

Q. Is there any *arithmetical* result of the higher policyholders' share percentage in this Exhibit 7 when you apply it to the balance of Schedule C?

A. Yes, the result is that other items of investment yield, as they emerge in Schedule C, are $114,502.27 which is roughly $11,000 less than the other items of investment yield as it merges in the Schedule C of the company's 1958 tax return.

Q. Is this as a result of the application of the different percentage found in Exhibit 7 as compared with the tax return?

A. Yes.

Q. Why is the percentage different, may I ask you?

A. The percentage is different solely because we excluded tax exempt interest in Exhibit 7 calculations.

Q. Drawing your attention to Schedule E of this Exhibit 7, which is the Phase 2 computation of gain from operations, can you explain the reason for a difference of the percentages of 91.12-plus percent for policyholders in this Exhibit 7, as opposed to 87.39-plus percent in the tax return?

A. Yes. The reason is that the required interest in our Exhibit 7 is identical with the required interest in the
42 company's tax return, because the required interest again depends only on tabular assumptions and the policyholders' share is equal to the required interest divided by the investment yield on Schedule A and we have reduced the investment yield in this exhibit by the exclusion of tax exempt interest.

Q. Applying that percentage which you have established in Exhibit 7 by excluding the receipt of the tax exempt income, applying that to the remainder of the formula for the Phase 2 computation for 1958, what is the result as compared with the gain from operations under Phase 2 under the tax return as filed?

A. The result is that in Schedule E in our Exhibit 7 we have included $76,099.50 which appears on line 7 of Schedule E, in Exhibit 7 calculations, as compared to $108,118.54 from line 7 of the company's 1958 tax return.

This difference is due solely to the fact that we have excluded tax exempt interest from our Exhibit 7 calculation and it results in a gain or a loss from operations in our exhibit, line 27, of $129,201.04 which is $32,019.04 less than the gain which appears in the 1958 tax return.

Q. And referring you, if you will, to Schedule E of the tax return, what was the amount of the policyholders' share of this gain from operations, excluded on line 4?

A. The amount excluded in the tax return was $32,019.04, which is exactly equal to the difference between the gain from operations in the 1958 tax return and in Exhibit 7.

Q. And you made no deduction in Exhibit 7, did you, on page 3-a, line 16, for wholly exempt interest?

A. No, because it was excluded entirely from the return.

Q. Is it fair to say that Exhibit 7 was prepared on the assumption that Atlas just didn't receive any interest from tax exempt bonds? A. Yes.

Q. Could it be on the same assumption that it had its amount of money represented by those tax exempt securities in an idle bank account? A. The result would have been exactly the same.

Q. Thank you. I hand you what has been marked for purposes of identification as Plaintiff's Exhibit 8, and ask you if you can tell us what it is, please?

A. Yes, I have a copy of it, and this is a calculation of the Atlas Life 1958 tax return as if it had not received $600.00 in interest, arising from Tulsa jail bonds.

Mr. SAUNDERS. Plaintiff offers Exhibit 8 into evidence.

43 Mr. HRDLICKA. Your Honor, I have the same objection which I previously stated. I would like to just make that a continuing objection for the record.

The COURT. You may do so and the record will so reflect, and the objection will be overruled.

(Plaintiff's Exhibit 8 was received in evidence; see page 12.)

Q. (By Mr. SAUNDERS.) Mr. Delaney, did the Atlas Life Insurance Company in 1958 have any Tulsa County jail bonds?

A. Yes, the Atlas Life owned $20,000 worth of Tulsa jail bonds on which it received $600.00 of interest in 1958.

Q. Was that $600.00 of interest in 1958 taken into account in the preparation of the tax return, Exhibit No. 6?

A. Yes, it was.

Q. I note in this Exhibit 8, which you now have before you, a number of inked notations. Can you tell us what those are, please?

A. Yes. The calculation in Exhibit 8 is made as if the Tulsa jail bonds had been in default and had paid no interest. The inked figures then show the changes which would have occurred in the company's tax return had this been the case.

You will note, for example, that on line 1—1–a of Schedule A—the inked figure is minus $600.00 which that is the change as the result of the fact that we have assumed the Atlas Life did not receive the $600.00 in tax exempt interest from these Tulsa jail bonds.

Q. And how is that reflected on page 1 as to the tax liability for 1958?

A. The tax liability shown on page 1 is $62,440.38 which is $175.00 less than the tax shown in the company's 1958 tax return.

Q. Did Atlas Life Insurance Company pay a tax of $175.00 in 1958 on the receipt of $600.00 interest from Tulsa County jail bonds?

A. Yes.

Mr. HRDLICKA. Your Honor, I am going to request that the last answer be excluded because it really constitutes a conclusion of law, because number one, the return under consideration was never filed. It's merely an exhibit. Number two, the witness' conclusion of what constitutes the imposition of tax is a question for the Court and not for the witness.

The COURT. Overruled.

44 Q. (By Mr. SAUNDERS.) Mr. Delaney, I hand you what have been marked for purposes of identification as Plaintiff's Exhibits 9 and 10. Can you tell me what they are?

A. Yes. These exhibits have been prepared to show the effect of including an extra $1000 of taxable investment income, that is exhibit that is marked as Exhibit 9, and Exhibit 10 shows the effect of including an extra $1000 of tax exempt interest.

Q. Do you have copies of those? A. Yes.

Mr. SAUNDERS. Plaintiff offers into evidence Plaintiffs Exhibits 9 and 10.

Mr. HRDLICKA. Same objection, your Honor.

The COURT. Haven't these been received in evidence before?

Mr. SAUNDERS. I was under the impression they had, your Honor, until just before the testimony of Mr. Delaney began.

The Government entered an objection to the relevancy and competency thereof and I felt it was appropriate to offer them again.

The COURT. They will be received in evidence.

(Plaintiff's Exhibits 9 and 10 were received in evidence; see page 12.)

The COURT. With the defendant's objection noted.

Q. (By Mr. SAUNDERS.) Can you explain to us the meaning of a marginal tax rate or marginal tax concept?

A. Yes. The marginal tax rate is the tax which would be paid on an additional $1.00 of income. Perhaps the clearest way to illustrate it would be to take the situation of an individual who earns $10,000 a year and we will say pays $1000 in income tax. The rate of tax is then 10%.

But if that individual were to earn an additional $1000 of income, his tax we will say would be increased to $1250 and thus on the additional $1000 of income he would have paid an additional $250.00 of tax, and we would say that his marginal tax rate is 25%.

Q. When identifying Plaintiff's Exhibit 9, you stated that you have prepared it to reflect the receipt of an additional $1000 of taxable investment income, and I note that on page 2 of the schedule of investment features of the company, some eight notations.

Is that to reflect $1000 additional taxable income?

45 A. Yes. In Exhibit 9 we have assumed that the company earned an additional $1000 income and this is shown by the ink figure on line, well, in the total figure for line 1, and on line 1–e of Schedule A.

Q. Then do the other inked figures on Plaintiff's Exhibit 9 reflect the result of this inclusion through the action of the formulas that you earlier went into detail concerning in the tax return?

A. Yes. The only change that is made in the company's 1958 tax return is to assume that we earned an additional $1000 and the inked figures in this Exhibit 9 show the changes which take place purely as the result of the mathematical calculations in their return.

Q. On Plaintiff's Exhibit 9, is there an increased tax liability reflected?

A. Yes, the line 6 of page 1 of this tax return, Exhibit 9, shows an increase in tax of $362.00 resulting from this increased

$1000 of income, and thus we would say that the marginal tax rate for Atlas Life was 36.2% on taxable investment income.

Q. Directing your attention to Plaintiff's Exhibit 10, I believe you identified same as saying it was prepared on the assumption that Atlas had received in 1958 an additional $1000 of tax exempt income. Do the ink figures on Plaintiff's Exhibit 10 reflect that in the appropriate schedules and do the ink figures also reflect the action of the formulas that you identified in detail in the tax return? A. Yes, they do.

Q. Did you make any other changes other than the inclusion of the $1000 wholly tax exempt income?

A. That was the only change that was made.

Q. What happened to the tax liability shown on page 1 of the return, assuming an additional $1000 of tax exempt income?

A. The total tax liability of the Atlas Life increased $291.00 as a result of the assumed $1000 increase in tax exempt investment income, and thus we would say that the Atlas Life has a marginal rate of 29.1% on tax exempt investment income.

Q. Have you ever served in an investment capacity in any of the companies by whom you are employed?

A. Yes, I served on the Investment Committee of the American General Life and on the Investment Committee of the Home State Life.

Q. As a member of the Investment Committee of these companies, can you tell us the objectives of those companies with reference to investments?

A. Yes. The objection of the committee is to secure the highest possible yield commensurate with the safety, liquidity and maturity.

Q. How do you determine the highest possible yield? You take into consideration any tax imposition?

46 A. Yes, we seek to secure the highest possible yield after federal income tax.

Q. How would you determine as a member of the Investment Committee whether to take cash and buy an interest paying security?

A. We would first determine the company's marginal tax rate and in effect we would prepare a pro forma tax return exactly as I have done in Exhibits 9 and 10.

Q. And from that could you tell the tax on the next additional dollar earned, in other words?

A. Yes, that would be the purpose of preparing that tax return.

Q. Now if two bonds are presented to an Investment Committee and you were serving on the Investment Committee, both of which constitute legal investments for life insurance companies and are identical as to call provisions, maturity and other factors, which bond would you select?

A. We would choose that bond that provided the highest after tax yield.

Q. Now using Plaintiff's Exhibit 9 which you state has a marginal tax rate for wholly taxable income of 36.2%, what would be the yield to the company on a 5% corporate rate security?

A. The net after tax yield to the company of a 5% corporate security purchased at par would be 3.19%, since the marginal tax rate is 36.2%.

Q. At what stated interest rate would Atlas, using the marginal rate concept of Plaintiff's Exhibit 10, have to purchase a municipal bond in order to have an equal yield?

A. Since the marginal tax rate shown in Exhibit 10 is 29.1% on tax exempt investment income, Atlas would need to secure a 4.5% yield on a tax exempt bond to have the equivalent after tax yield.

Q. In your experience as an investment officer, is it your judgment that an insurance company would be able to buy a state or local bond yielding 4.5% of the same grade as an industrial bond yielding 5%.

A. No, under normal market conditions the spread would be greater than that and the company if it chose to buy the municipal bond would have to select a lower grade bond. More likely it would buy the corporate obligation.

Q. Mr. Delaney, I hand you what has been marked for purposes of identification as Plaintiff's Exhibit 11 and Plaintiff's Exhibit 12. Can you tell us what those are? A. Yes, I have copies of these.

Exhibit 11 is a computation of the Atlas Life 1958 income tax based upon the 1942 law in which we have included all of the company's tax exempt investment income.

47 Exhibit 12 is an identical calculation based on the 1942 law but in this case we have excluded all of the company's tax exempt income.

Mr. SAUNDERS. We offer into evidence Plaintiff's Exhibits 11 and 12.

Mr. HRDLICKA. Same objection, your Honor.

The Court: Objection overruled. Plaintiff's Exhibits 11 and 12 will be received in evidence.

(Plaintiff's Exhibits 11 and 12 were received in evidence; see page 12.)

Q. (By Mr. SAUNDERS). I believe you stated, Mr. Delaney, that you have been preparing life insurance company income tax returns for ten years? A. Yes.

Q. Has some of that period involved the application of the 1942 Act? A. Yes.

Q. And these computations that you have before you, as Plaintiff's Exhibits 11 and 12, were made for the Atlas figures, numbers, books and records for 1958 but applying the 1942 Act; is that true?

A. That is true, and using the Treasury decision, whose number I forget at the moment, but which establishes the secretary's ratio for 1958.

Q. Is there any difference in tax liability between Plaintiff's Exhibit 11 and Plaintiff's Exhibit 12?

A. No, the tax liability which occurs on line 5 of page 1 of both returns is identical and is equal to $56,906.36.

Q. As an expert and as having prepared these tax returns, do you have an opinion for the reason that the two computations, Plaintiff's Exhibit 11 being based upon the presence of tax exempt interest and the computations of Plaintiff's Exhibit 12 being based on the absolute exclusion or absence of tax exempt interest, ending up in the identical tax liability?

A. Yes, Exhibit 11 which includes the tax exempt interest in this calculation as provided by the 1942 law, the tax exempt interest is included but it is fully deductible as provided by law. Thus the end result is exactly the same as the calculation in Exhibit 12 where we omitted the tax exempt interest completely.

Q. Mr. Delaney I hand you what has heretofore been introduced and received into evidence as Plaintiff's Exhibit 1, the annual statement of Atlas Life Insurance Company for 1958, and ask you to turn to page 4 and tell us if that return reflects the company's net gains from operations?

48 A. Yes, line 33 at page 4 shows a net gain from operations for the company of $248,220.87.

Q. The tax return for the company heretofore introduced and received into evidence as Plaintiff's Exhibit 6 indicates a gain from operations, does it not?

A. Yes, and the gain from operations as shown by the tax return is $161,220.08.

Q. Now Mr. Delaney, we are talking about contrasting the annual statements and this tax return with reference only to the Phase 2 tax computation, is that correct? A. Yes.

Q. Why is the total in the annual statement on page 4, some $248,220.00, and the gain from operations for federal income tax purposes less, being $161,220.00?

A. The reason is that there are certain items which are deductible for annual statement purposes but are not deductible for federal income tax purposes. An example would be federal income tax.

There are other items which are deductible in the annual statement that are not deductible for federal income tax—I'm sorry, reverse that and say there are other items which are deductible in the federal income tax return but are not deductible in the annual statement.

An example of these items would be the small business deduction and the deduction for non-participating insurance.

Q. You stated that you had seen the Revenue Agent's report at the conclusion of the audit for 1958. Is there a reconciliation sheet in that audit which reflects the differences of inclusion or exclusion or deductibility or includability between the annual statement and the tax return as filed? A. Yes, there is.

Q. I hand you what has been marked for identification as Plaintiff's Exhibit 13 and ask you what it is?

A. This is a reconciliation between the net gains from operations in the annual statement and the gain from operations in the tax return.

Q. And this is the appropriate page from the Revenue Agent's report; is that true? A. Yes.

Mr. SAUNDERS. We offer into evidence Plaintiff's Exhibit 13.

The COURT. Plaintiff's Exhibit 13 will be received in evidence with the defendant's objections noted.

(Plaintiff's Exhibit 13 was received in evidence; see page 12.)

49 Q. (By Mr. SAUNDERS.) In this reconciliation statement, Plaintiff's Exhibit 13, Mr. Delaney, can you tell us what increases you made and what deductions you made?

A. Yes. I started from the net gain from operations in the

annual statement of $248,220.87 and added to this those items which are deductible for statement purposes but not deductible for federal income tax purposes, such as federal income tax itself. The total of these items was $184,133.76, and thus the total gain from operations to this point was $432,354.63.

Q. And that's shown on the left-hand column marked Annual Statement, is that true, on Exhibit 13? A. Yes.

Q. How does this increased amount in the annual statement relate to the gain from operations in the tax return for 1958?

A. From this increased amount again, it is necessary to deduct those items such as the small business deduction, which are deductible for tax purposes but not for annual statement purposes. The total of these items, excluding any deduction for tax exempt interest, was $266,515.80, bringing us to a gain for tax purposes before any adjustment for tax exempt interest of $165,838.83.

Q. Did you make any further computations covering this amount of $165,838?

A. Yes. From this amount I deducted the company's share of tax exempt interest and the resulting amount is $161,220.08, which is exactly equal to the gain from operations as it appears in the tax return.

Q. What is the dollar amount of the company's share of tax exempt interest that was deducted in this Plaintiff's Exhibit 13?

A. $4,618.75.

Q. Is that same amount reflected as a deduction in the tax return as filed in Schedule E?

A. Yes, as the company's share of tax exempt income.

Q. Other than this deduction of $4,618.75, did you make any other calculation or computation or treatment of the tax exempt interest? A. No.

Q. As an expert in preparation of life insurance company income tax returns under the 1959 Act, do you have any opinion as to why the tax that is incident, if any, with reference to the balance of tax exempt interest received by Atlas during 1958, in Schedule E of the tax return is known as the company's share, $32,019.04, what is the incidence if any with reference to that from this reconciliation?

A. Since the gain from operations from the annual statement includes all items of tax exempt interest and since we have been able to reconcile that back to the gain from operations as shown in the tax return by deducting only the company's share of tax

exempt interest. $4,618.75, I conclude that the tax return has included in its gain from operations the balance of the tax exempt investment income simply as a matter of arithmetic, and that balance was some $32,000.

50 Q. Now directing your attention to Plaintiff's Exhibit 7, heretofore received in evidence, can you take these reconciliation figures and make a computation with reference to the tax liability shown on Exhibit 7?

A. Yes. Beginning again with the figure of $165,838.83 which was the gain from operations before any adjustment for tax exempt interest, I deduct from that figure the full amount of the tax exempt interest which the company received, $36,637.39 and this gives me a figure of $129,201.04 which is exactly equal to the figures shown on Exhibit 7 as the company's gain from operations.

Q. As an expert, do you have an opinion as to why the reconciliation approach with reference to the Revenue Agent's summary sheet and the Plaintiff's Exhibit 7, after excluding all the tax exempt interest, is as the figure of $161,220 for the taxable gain as appears in the return, if that is what occurred?

A. Yes, both—because both in the reconciliation and in Exhibit 7 we have excluded tax exempt interest completely, has no effect.

Q. I hand you now, Mr. Delaney, what have been marked for purposes of identification as Plaintiff's Exhibits 14, 15 and 16 and ask you to tell us what they are?

A. I have copies of these. Exhibit 14 is a calculation of the 1958 tax return of the Atlas Life, including the company's tax exempt interest in determining the policy and other contract liability requirements but deducting 100% of such tax exempt interest in computing the taxable investment income, as well as deducting all of the policy and other contract liability requirements.

The calculation follows the form of the tax bill as originally passed by the House, H.R. 4245.

Q. Is that before or after what is known as the "Add Back Provision"?

A. Before the Add Back Provision which was provided by that House bill.

Q. Tell us what is Plaintiff's Exhibit 15.

A. Plaintiff's Exhibit 15 is exactly the same calculation as was made in 14 except that in this case we have provided for the "add back" which was called for by that bill.

Q. And what is Plaintiff's Exhibit 16?

A. Plaintiff's Exhibit 16 is again a calculation under the House Bill but this time we have excluded tax exempt interest in computing the policy and other contract liability requirements, and we have also excluded the add back.

51 Mr. SAUNDERS. Plaintiff offers into evidence Exhibits 14, 15 and 16.

Mr. HRDLICKA. Same objections, your Honor.

The COURT. The defendant's objection will be overruled. Plaintiff's Exhibits No. 14, 15 and 16 will be received in evidence.

(Plaintiff's Exhibits 14, 15 and 16 were received in evidence; see page 12.)

Q. (By Mr. SAUNDERS.) Directing your attention to Exhibit 14, Mr. Delaney, what is the tax liability shown for Atlas under this computation? A. Tax liability shown is $46,161.11.

Q. Please compare this Exhibit 14 with the tax return as filed, being Exhibit No. 6, as to type of investment yield, policyholder and other contract liability requirements and the computation of tax.

A. The investment yield in this Exhibit 14 is identical with the investment yield in the company's 1958 tax return as filed. The policy and other contract liability requirements are identical also with the policy and other contract liability requirements in the exhibit as filed.

Q. In the tax return as filed, is that true?

A. In the tax return as filed. Excuse me.

Q. In other words, both the tax return as filed and Exhibit 14 included the full amount of tax exempt interest received in 1958?

A. That's correct.

Q. Are there any changes in the computation of the tax under Schedule C between this exhibit and the tax return as filed?

A. Yes. Schedule C in this exhibit deducts the full amount of tax exempt interest, $36,637.79, while the 1958 tax return deducts only the company's share of such tax exempt interest.

The same thing is true in Exhibit E—in Schedule E, excuse me, in Schedule E where again we have deducted the full amount of tax exempt interest, where the tax return deducted only the company's share.

Q. The Schedule E you referred to is the gain from operations for Phase 2 computation, is that true?

A. Yes. We might note also that in Schedule E the required interest is the same for this Exhibit 14 and for the tax, 1958 tax return as filed, because again that required interest depends only on tabular assumptions and has no relation to the company's investment experience.

52 Q. Or the source of the investment income of the company?

A. Yes.

Q. Turning your attention to Exhibit 15, can you contrast that with the tax return as filed?

A. The tax liability as shown on page 1 of Exhibit 15 is $62,615.05, and is identical with the tax liability as shown in the 1958 tax return.

Q. Did Exhibit 15 include in investment yield all of the tax exempt income as did the tax return?

A. Yes, it did. The investment yield is identical with the two exhibits and it is the policy and other contract liability requirements. However, in Exhibit 15 in Schedule C, instead of deducting the entire policy and other contract liability requirements, we have reduced that reduction by the ratio of the policy and other contract liability requirements to the investment yield times the tax exempt interest.

In other words, we have deducted from the policy and other contract liability requirements a share of the company's tax exempt interest.

Q. Why did you do that in the preparation of this Exhibit 15?

A. That is the provision that was called for by the House Bill as originally passed.

Q. Were those Sections 805–E and 809 of H.R. 4245 as it originally passed?

A. Yes, they are. We did not discuss the fact that we made a similar reduction in Schedule E which is called for by the 809 section, and reduced the required interest in this case by a share of the company's tax exempt investment income.

Q. I believe you stated that using the adjustments called for under H.R. 4245, you arrived at the same taxable income as the tax return as filed?

A. That is correct.

Q. Turning your attention to Exhibit 16, can you contrast that with the tax return as filed?

A. Yes. In Exhibit 16 we have again made a calculation, following the format of the House Bill 4245 but this time we

have excluded entirely tax exempt interest from the investment yield.

Q. Did you make a further treatment of tax exempt income in the computation of the taxable investment income in Schedule C?

A. Yes. Then in Schedule C we have reduced the policy and other contract liability requirements by an amount of $20,006.73.

Q. Why did you do that?

A. The policy and other contract liability requirements, which emerged as a mathematical process when we eliminated the tax exempt income, was $20,006.73 less than the policy and other contract liability requirements emerging when we included tax exempt interest.

53

Thus, by excluding this $20,000 from the policy and contract liability requirements, we have completely eliminated that part of the policy and contract liability requirements which came about as a result of the receipt of tax exempt investment income.

Q. Now what is the tax liability shown on this Exhibit 16?

A. Tax liability shown here is equal to $51,362.86 and this is identically the same as that in our Exhibit 7.

Q. Directing your attention once again to Plaintiff's Exhibit 16, did you make any adjustment in the gain from operations Phase 2 computations?

A. No, I did not, because in this case the required interest did not depend in any way upon the company's receipt of tax exempt income, and thus it was not necessary to make any adjustment. Again, the gain from operations as it emerges in Schedule E is identical to the gain that emerged in our Exhibit 7.

Mr. SAUNDERS. Thank you, Mr. Delaney. You may inquire.

Cross-Examination By Mr. HRDLICKA:

Q. Mr. Delaney, I understand that you did not prepare the actual original returns for the company filed for the year 1958, is that correct?

A. Yes.

Q. But you did on the basis of that return as filed and adjustments that were agreed upon by the parties, you did prepare what we have been referring to as Exhibit No. 6, is that correct?

A. Yes.

Q. This exhibit right here?

A. Yes.

Q. And did you say that this exhibit—I believe you testified that this exhibit was computed under the directions for computing life insurance company taxable income as prescribed by the regulations, is that correct?

A. Yes.

Q. And by that do you mean that the item referred to as investment yield as determined and as allocated between policyholders and the company in arriving at the taxable income was taxable investment income for a life insurance company; is that basically the formula that was used?

A. Yes. The Schedule C excludes a share of the investment yield equivalent to the policyholders' share as calculated in the return.

Q. Now Exhibit 7, Mr. Delaney, or in Exhibit No. 7 you exclude from consideration completely all tax exempt interest is that correct?

A. Yes.

54 Q. Could you tell me what section of the 1954 Code that you relied on in doing that, what Code section governs your computations under this exhibit?

A. I believe 103–A but I would say only that I excluded the tax exempt interest in making the calculations.

Q. When you refer to Section 103 you are talking about the section that excludes from taxation interest received on certain bonds, municipal bonds and other local obligations, isn't that correct? A. Yes.

Q. What I am asking you, is there any specific section within the life insurance company income tax Act of 1959 which directed your exact method of computation, computing income tax as reflected in Exhibit No. 7?

A. I would say that the exception clauses were the basis on which that calculation was made.

Q. The exception clauses in Sections 804 and 809 which you are referring to? A. That's right.

Q. Well, going back then to Exhibit No. 6, do you recall Exhibit No. 6? A. Yes.

Q. Isn't it true that Section 804–A of the Internal Revenue Code of 1954, which I am showing you here, has a section which defines or deals with the exclusion of policyholders' share of investment yield? A. Yes.

Q. And isn't it Section 804–A that you would rely upon then in determining what percentage of total investment yield

should be excluded to policyholders? A. Certainly in following the tax return.

Q. Well, then my question to you is that with reference to Exhibit 7, is there any Code section similar to Section 804–A—I'm not talking now about the exception clauses—any section similar to 804–A in this Act which you followed in excluding from consideration entirely the tax exempt interest? A. Only the exception sections.

Q. Only the exception sections. Would that same be true, Mr. Delaney, of Exhibit No. 8?

A. Exhibit 8 was an illustrative exhibit to show that if the Tulsa jail bonds had been in default in the year 1958, that the tax paid by Atlas would have been less.

Q. I see. Then this is just on an assumption that something may have happened which didn't happen, is that correct? A. Yes.

Q. I mean this is not based on what actually did happen to to the company?

A. No. The company did receive $600.00 from Tulsa jail bonds.

Q. And then Exhibit 8 is computed following the regulations, as I understand it, but on the assumption that the company did not receive the $600.00? A. That is correct.

55 Q. Exhibit 9 then is a similar type of exhibit, isn't that correct, but the assumption here is that they received an additional $1000 of tax exempt interest; was that it?

A. Yes, the purpose of Exhibit 9 was to develop the company's marginal rate.

Q. But here again Exhibit 9 is computed on the basis of the Code and Regulations as they exist, is that right?

A. Yes, this is the kind of calculation the company would do to determine the tax they would pay, in making its investment decisions.

Q. What about Exhibit 10?

A. Exhibit 10, again, was an exhibit designed to show the effect of the marginal tax rate on tax exempt interest.

Q. And again this exhibit follows the same basic Code provisions as Exhibit No. 6, is that correct? A. That is correct.

Q. Now as I understood your testimony, Exhibits 11 and 12 were based upon the law that was in effect in 1942, is that correct?

A. Yes.

Q. And did you mean, did you compute this on the basis of the '42 Act as it applied to the year 1958 or as if it had applied to the year 1958? A. As if it had applied during 1958.

Q. Were you in computing Exhibits 11 and 12, were you applying the 1942 Act to the extent that it actually applied to the year 1957, or did you mean to apply just the '42 Act as it existed in '42?

A. We applied the '42 Act as it existed to the company's 1958 figures.

Q. Yes, but I mean was it the '42 Act as originally enacted or the '42 Act as amended?

A. No, it was the '42 Act as originally enacted.

Q. As originally enacted? A. Yes.

Q. I see. And your computations then in Exhibits 11 and 12 were based upon that Act? A. That is correct.

Q. Are these computations based in any way upon the Internal Revenue Code of 1954, the Life Insurance Company Income Tax Act of 1959?

A. Now I want to be sure. You mentioned 1954. You were talking about 1959?

Q. Yes. While I am talking about the 1954 Code, which includes the life insurance——

A. (Interposing.) No, no relation to the Life Insurance Company Income Tax Act of 1959.

Q. Then Exhibits 14 through 16, as I understand it, were based on the House Bill which had been considered at one point before adoption of the Life Insurance Company Act of 1959, but which was never passed, is that correct? A. That is correct.

56 Q. Mr. Delaney, might I ask when you made all these computations that we have seen in these various exhibits?

A. Well, at various periods of time. As you would guess, it takes a long time.

Q. How long ago did you make these calculations?

A. They have all been made subsequent to the Revenue Agent's report.

Q. Subsequent to the Revenue Agent's report?

A. They incorporate all of the changes that were made as a result of that report.

Q. Have you made computations similar to these computations with respect to other insurance companies prior to the time that you made these? A. Yes.

Q. Have you ever prepared exhibits similar to the ones we have now been looking at for the purpose of demonstrating possible differences between the Life Insurance Company Act of 1959 as opposed to the 1942 Act, or the House Bill that was considered in the 1959 Act? A. No.

Q. This is the first time you have prepared this type of exhibit? A. Yes.

Q. For that purpose. Mr. Delaney, since the Exhibit No. 7 in particular is not based upon—I am not speaking now of the exception clauses in the 1959 Act, but Exhibit No. 7 is not based upon the '42 Act or the House Bill and as far as I can determine it is not founded upon any particular provisions of the 1954 Code except the exception clauses, so whose decision was it to exclude the tax exempt from these computations? I mean whose idea was that?

A. This was my own idea. At the time the 1959 bill was passed, the exception clauses do provide that if it can be shown that tax investment income is taxed, adjustment shall be made and I think that by excluding it we find out whether or not it has been taxed. I think it has been taxed.

Q. Did you submit any of these computations to the Congress while it was considering the House Bill or Senate Bill?

A. Certainly I discussed these with people who were talking with—particularly Mr. Stanley Hill who was in Washington at this time.

Q. So that as far as you know, these computations were brought to the attention of Congress at the time it considered the Act?

A. I can't testify to my own knowledge about that.

Mr. SAUNDERS. If the Court please, I believe this is outside the scope of the direct examination and improper cross-examination.

57 The COURT. Well, overruled It's testing his experience with reference to these exhibits; 11, 12, 13, 14, why he made them and so forth.

Mr. HRDLICKA. Your Honor, I would just add that as complex as these computations are, it would be pretty hard for me to get outside the scope of direct examination. I think almost anything would apply to those.

Q. (By Mr. HRDLICKA). Mr. Delaney, are there any additional approaches that could be made to this problem except for the ones that you have presented here? I mean are there other possible ways you could rearrange the tax exempt interest and the various formula, allocation formula, and other items to make similar types of adjustments as you have demonstrated in your various exhibits here?

A. None that I know of.

Q. Well, do you think that as a mathematician or if you studied that you might devise additional ways of readjusting the allocation formula? I mean do you think you have exhausted the mathematical possibilities in treating these various items by the exhibits you have offered here?

A. I think we have exhausted reasonable possibilities.

Q. These exhibits then I take it represent all the possibilities you could think of?

A. Not all that I could think of, all the reasonable, all the reasonable ones.

Q. Did you make, did you consider making other computations based upon other hypothetical information, not the actual information of this company, but other hypothetical information that might apply to any insurance company?

A. Let me answer that by saying we make similar calculations to these in our own companies for purposes of determining our tax, yield after taxes.

Q. Well, isn't it possible for an insurance company, for example, to have a particular income structure so that by computing the company's tax the way you have demonstrated it in your Exhibits 7 and 14, would actually lead to a greater tax than what you have shown on those exhibits? I mean aren't there some times when you apply those principles of excluding tax exempt interest that you would actually come up with a greater tax than if you included the items in the computations?

A. I couldn't say that it was impossible. I would think it is very unlikely. Not in my experience has that arisen.

Q. Have you ever tried any computations along those lines to see if that would be possible?

58 A. We have in several companies made calculations similar to these, and that situation has not arisen.

Q. I believe that your Exhibit 14 is the one that reflects the greatest amount of tax refund, is that correct?

A. Yes, I believe so, that's the one that is the greatest.

Q. Now tell me this, if you assumed that this company's, all of the assets and all of the figures reflected in this return, were exactly the same as they are in Exhibit 14 but you assume further that the company had received no tax exempt interest whatsoever, in other words that it owned no tax exempt bonds but it still had the same amount in dollars of investment yield—do you follow my question so far?

A. Let me get with it. If we assume that all of the company's—the identical investment yield but no tax exempt interest?

Q. Right, but no tax exempt interest. A. Yes.

Q. And all other things being equal, would the tax be higher or less than that reflected in Exhibit 14, do you know?

A. The tax would be more than that reflected in Exhibit 14.

Q. Would be more than that reflected. So that in effect even in the most favorable computation here, the inclusion of tax exempt interest does result in a decreased tax?

A. No, Exhibit 14 is a calculation in which we have included tax exempt interest and its effect on the policy and other contract liabilities deduction, and have in effect then got the benefit of double deduction.

Q. I'm sorry, Mr. Delaney, my mistake. I was at the wrong end of the scale.

I want you to examine Exhibit 6, which shows the actual tax liability as reflected in the return originally filed. A. Yes.

Q. Now making the same assumption, that you have the same amount of investment yield but that you no tax exempt security, and that all other items in the return are the same, would the tax be greater or less than as reflected in that return, Exhibit No. 6?

A. The tax would be slightly greater. We are assuming here that we replace the $36,000 of tax exempt by $36,000 of fully taxable income.

Q. Right. I am assuming that there would be no side effect on policy and other contract liabilities or your earnings rate or anything like that?

A. Right. The tax would be slightly greater. Specifically, the Schedule C, taxable investment income would be increased by $5,372.42 which is the company's share of tax exempt interest, and Schedule E would be increased by $4,600—$4,618.75.

Q. I see. Thank you.

59 Mr. Delaney, I believe that you testified with respect to Exhibit No. 7 where you completely excluded tax exempt interest, you came up with a slightly different adjusted life insurance reserve and a slightly different adjusted reserve rate, is that correct?

A. That is correct.

Q. That is shown on Schedule E.

A. Well, it is shown here on Schedule B.

Q. On Schedule B. I'm sorry. This is not too clear.

Now in Part 2, entitled "Assets," did you exclude the tax exempt securities from assets or were they allowed to remain in assets?

A. They were allowed to remain in assets. We assume in effect that the tax exempt securities had not earned any money, that the money was perhaps lying in the bank idle.

Q. They existed as assets but earned no income, is what your assumption was? A. Yes.

Q. Now that assumption under your computations led to a policyholder's share under Section 804 of 86.649%, which is reflected on page 3, is that right? A. Yes.

Q. Schedule C, line 1? A. Yes.

Q. Which is a slight increase over that same percentage reflected in Exhibit 6, isn't that correct? A. Yes.

Q. Now that increase or that percentage is applied to all investment yield, isn't that right?

A. Yes. In this case we have already excluded the tax exempt interest.

Q. Right, so that——

A (Interposing). Confines this percentage to a smaller total investment yield.

Q. You are in effect putting over to the policyholders a greater percentage of investment yield that remains after the tax exempt securities or tax exempt income is taken out of investment yield, isn't that correct? A. Well, this is simply a mathematical calculation.

Q. Right. A. Excluding tax exempt interest.

Q. But the end result is that the greater percentage is excluded and attributed to the policyholders' share?

A. The end result is that we do secure a larger exclusion for other items of investment yield.

Q. And of course the greater percentage of investment yield that is attributable to the shareholders, the less that is taxed to

the company, isn't that correct? I mean that just follows as a mathematical——A. Please state that again.

60 Q. I say the greater percentage of the investment yield that is attributed to the policyholders, the less the percentage that is taxed to the company, isn't that correct?

A. The less is the company's share, I'll certainly agree to that.

Q. Was it your testimony that the assumed interest rate has no bearing whatever on the actual interest rate or no relationship whatever to the actual interest rate?

A. In the tax form, certainly, there is a very loose relationship between when a company establishes the basis of its reserves, of course it is restricted by the statute in the interest rate it can assume, also usually has some loose relationship to its actual investment earnings, but there are many other factors to be considered as well.

Q. Well, isn't the assumed interest rate applied to investment assets to try and anticipate the earnings on those assets for future years, to be added to reserves? A. I would say no.

Q. How is the assumed interest rate applied?

A. The life insurance reserves increase each year by an amount equal to the assumed interest rate times the reserve. There is increase in reserve as a result of the interest assumption. I might say it that way.

Q. So you apply your assumed interest rate to the reserves and that will give you an increase in the reserve for the following year, is that correct?

A. That is part of the increase in reserve, that part attributable to interest.

Q. Then there are other factors that also affect the reserve itself, is that correct?

A. Yes, the net premium and the valuation basis and so forth.

Q. Now with respect to, I believe it was Exhibit 7 on the Phase 2 computation on Schedule E, a question was asked you whether—I am not sure I've got the right exhibit here but I think you can correct me if I don't—a question was asked you whether the tax exempt interest had any effect, or the actual interest rate on tax exempts had any effect on the computation reflected in Schedule E, and I believe you stated it didn't, is that correct?

A. *I* has no effect on the required interest.

Q. The required—what is the reason for that?

A. Required interest is based on tabular assumptions, the assumed interest rate, the assumed reserve structure.

Q. So in that respect the tax exempt securities are no different than any other security, are they?

A. That's correct. The receipt of any investment income has no effect on this required interest.

61 Q. So what you really are stating then in a broader sense is that this is computed on the basis of an assumed interest rate, which is not necessarily the same and really has no relation to, except the one you have previously explained, to the actual earnings rate?

A. That is correct.

Q. Mr. Delaney, I have only one further question I would like to ask you. You testified with respect to certain marginal tax computations and in connection with that you showed how certain different treatment of certain items can affect tax liability. Isn't it true that there are a lot of different items that can affect tax liability of an insurance company? Let's say for example that an insurance company, all other factors remaining equal, if it merely increased its cash on hand, idle cash on hand, could you tell us what effect that would have on that company's liability under the '59 Act?

A. I am not sure how would it—how it would increase its cash on hand.

Q. Well, I'm talking about, it would be an increase on hand, it would be included within assets under Section 805?

A. It would have to effect this increase in some way. Would it sell some of its security?

Q. I was attempting to maintain the investment yield the same and so I didn't want to have—let's assume there is a sale of an item which had not previously been included in the definition of assets under Section 805 and a sale of that type of item was made and the idle cash was in the bank, so in effect you had an increase of assets under Section 805, but no increase in investment yield.

What would the effect of that be on the company?

A. This would cause a slight increase in tax.

Q. Slight increase in tax. And aren't there a lot of other items similar to this which could affect the company's tax even though there is no actual difference in the company's income? For example, idle cash produces no more income but yet with

the addition of idle cash you would have a greater tax under the Act. Aren't there other types that would have the same effect?

A. There might be. I can think of none.

62 ROBERT D. ALLEN, called as a witness on behalf of the plaintiff, being of lawful age and having first been duly sworn, testified as follows:

Direct Examination By Mr. SAUNDERS:

Q. State your name, please. A. Robert D. Allen.

Q. Where do you live, Mr. Allen? A. Oklahoma City.

Q. What is your occupation?

A. I am the Assistant Insurance Commissioner, Chief Counsel, the Oklahoma Insurance Department.

Q. How long have you held that position?

A. Slightly over five years.

Q. What, generally speaking, are your duties in that position?

A. Well, the Commissioner's office, we handle the licensing of all companies. That includes life, casualty and property. That's originally applying companies, and also the renewal licenses annually. We collect the annual premium taxes, conduct examinations of all companies domestic, participate in the examination of all foreign companies doing business in Oklahoma from time to time.

Also I have general house counsel responsibility with the Commissioner's office.

Q. In connection with the performance of your duties, are you familiar with the statutory reserve requirements of the State of Oklahoma with reference to life insurance companies in Oklahoma?

A. Yes, I am. The life reserve requirements as set out in Section 1510, Title 36, Oklahoma Statutes 1961.

Q. From the standpoint of the Insurance Commissioner's Office and the performance of your duties, what are the life insurance reserves that are determined under the Oklahoma statutes?

A. Well, all policy reserves are liabilities of the company under our statute.

Q. Are they determined under actuarial tables?

A. Well, yes, the determination of the reserves is made on the basis of the classes of policies, the actuarial tables employed, and the interest assumed. They vary from classes of business.

Q. In your opinion, what is the purpose of having a life insurance company estimate or calculate its insurance liability annually and then include them in an annual report filed in your office?

A. Well, of course our purpose is, it's a statutory requirement and it is a test to determine the solvency of the company and its eligibility to transact insurance. The liabilities, policy liabilities are deducted from their admitted assets. We have a statutory minimum capital and surplus which the company has to maintain in order to hold its license.

63 Q. Are the reserve liabilities of Oklahoma insurance companies reflected on the books of the Oklahoma companies?

A. No, the only way you can get into a determination of that is by an inventory of the business in force.

Q. And you would apply the proper—— A. Statutory test.

Q. Is there any requirement of the Oklahoma Insurance Department with reference to a company segregating or earmarking assets to meet it reserve liability?

A. No, not only is there no requirement that they segregate, we would not permit segregation of the company's assets, they stand for all the liabilities of the company.

Q. How does the Oklahoma Insurance Department conduct an examination of an insurance company, in particular Atlas?

A. I think Atlas just went through one. I believe that—well, of course there are field audits. They are very comprehensive. Primarily our examiners are, we try to draw on ex-FBI people and men of some repute and ability in accounting. It's about like a federal bank examination. We count, physically count securities, verify accounts as necessary to determine their verity. It's a field audit.

Q. Are you checking their assets among other things?

A. Well, the purpose of it is to determine assets and liabilities.

Q. Can you explain, Mr. Allen, in general terms the Oklahoma statutory requirements as to investment by life insurance companies?

A. Well, our investment statutes as they pertain to life insurance companies are in the nature of limitations. Investment policies are the responsibility of the management of the company and we have percentage limitations that apply to various classes of investment, with certain exceptions. A

company may invest any of its funds in U.S. Government obligations, general obligations of states and municipalities. In other areas, like corporates, common stocks, there are percentage limitations that are applied against the company's admitted assets.

Q. Can a domestic Oklahoma life insurance company invest in a corporate stock which does not pay cash dividends, pays dividends in stock?

A. Our statute requires that any stock that the company invests in be dividend paying. As far as the requirement being a cash dividend, it is not so expressed in the statute. We wouldn't require it. There is a test with respect to earnings. They have to earn a certain ratio available for dividends against fixed charges to be an eligible investment, but they have to be dividend paying, but that would not necessarily have to be a cash dividend.

64 Q. Mr. Allen, do you know the purpose of these investment requirements in the Oklahoma Insurance Code?

A. Well, you can tell pretty well from considering them, but the Legislature in Oklahoma wants the companies operated on a conservative basis and it gives them actually an enforced and broad investment base on which to operate that company, without getting into specific investments.

Q. Does the Insurance Commissioner's Office ever recommend that a life insurance company change the type of its investments, assuming that it is operating within the statutory requirements?

A. No, investment policies are the responsibility of management except we have these limitations on the classes of securities that they can get into and the amounts which can be invested, but that's the only limitation.

Q. Mr. Allen, does your department ever question the company's investments if the rate of return on the investments aggregate during the year does not equal or exceed the interest rate assumed by the company in computing these reserves?

A. Actually we don't concern ourselves with the company's investment yield or rate of return as such, unless it is a situation where solvency is threatened. The answer to your question would be "no, we don't."

Q. Would a growth stock that paid no dividends be a qualified investment for the purpose of determining solvency?

A. A growth stock that paid no dividends?

Q. Uh huh.

A. Under our statute, unless it was a dividend paying security, the company would not be authorized to invest in it.

Q. After an investment had been made in authorized stock but then if it stopped paying dividends but it was a growth stock, appreciating in value, is my real question, Mr. Allen, is that a permitted asset?

A. Well, certainly, eligibility of an investment under our statute is determined as of the date of acquisition, if they cease paying dividends later on it would still be carried as an admitted asset.

Q. And would the value of that stock, whether or not it paid dividends, be included in a test for solvency? A. Certainly.

Mr. SAUNDERS. I believe that is all.

Cross-Examination By Mr. HRDLICKA:

Q. Mr. Allen, what action is taken by the Insurance Commissioner's Office in the event an insurance company has assets insufficient to meet its reserves?

65. A. Well, if it has assets which are insufficient to meet any of its liabilities, we have—if it is impaired less than 20%, we give them sixty days' notice to make restoration. If it is impaired more than 60%, pardon me, more than 20%, then we are required to take some type of rehabilitation action.

Q. And what might that include?

A. Oh, it could be a *conservership* or a receivership.

Mr. SAUNDERS. This concludes the presentation of plaintiff's case, your Honor.

The COURT. Very well. Let the record show that the plaintiff rests its case.

* * * * *

The COURT. Let the record show that defendant rests its case. Does counsel care to make an argument in this case?

66–74. * * * * *

[Clerk's Certificate to foregoing transcript omitted in printing.]

IN UNITED S....S DI....T COURT for the northern District

Plaintiff's Exhibit 6

FORM 1120 L — U.S. LIFE INSURANCE COMPANY INCOME TAX RETURN — FOR CALENDAR YEAR 1958

PLEASE TYPE OR PRINT PLAINLY

The Atlas Life Insurance Company

415 South Boston Avenue, Tulsa 1, Oklahoma

September 25, 1918 Oklahoma

01-05132

35,485.55

Not applicable to this company

430,508.05

☐ Yes ☒ No

☐ Yes ☒ No

☒ Yes ☐ No

☐ Yes ☒ No

LIFE INSURANCE COMPANY TAXABLE INCOME

1. (a) The taxable investment income (Schedule C) 100,760.87
   (b) The gain (loss) from operations (Schedule D) 161,229.68
   (c) The smaller of (a) or (b) 100,760.87
2. 30 percent of the excess, if any, of (b) over (a) 30,229.02
3. Life insurance company taxable income (Total lines 1(c) and 2) tax treatment used 130,989.89

COMPUTATION OF TAX DUE OR REFUND

4. If amount of line 3 is:
   (a) Not over $25,000—
   Enter 30 percent of line 3 (22 percent if a consolidated return)
   (b) Over $25,000—
   Enter 52 percent of line 3 (54 percent if a consolidated return) 68,115.05
   Subtract $5,500, and enter difference 5,500.00 62,615.05
5. Less: Credit allowed a domestic corporation for income taxes paid to a foreign country or United States possession (Submit Form 1118)
6. Total income tax (line 4 less line 5) 62,615.05
7. Credits for amounts paid on 1958 income tax:
   (a) Tax paid with application for extension of time in which to file 64,055.79
   (b) Payments and credits on 1958 Declaration of Estimated Tax 64,055.79
8. If tax (line 6) is larger than payments (line 7), the balance is TAX DUE. Enter such balance here
9. If payments (line 7) are larger than tax (line 6) Enter the OVERPAYMENT here
10. Enter amount of line 9 you want: Credited on 1959 estimated tax 0
    Refunded 1,440.74

SIGNATURE AND VERIFICATION (See Instruction E)

Declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined and to the best of my knowledge and belief is a true, correct, and complete return. If the return is prepared by a person other than the taxpayer, his declaration is based on all the information relating to the matters required to be reported in the return of which he has knowledge.

CORPORATE SEAL

(Date) (Signature of officer) (Title)

(Date) (Individual or firm signature) (Address)

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EXHIBIT 1 PX 6 FORM 1120 L—1958

SCHEDULE A—INVESTMENT YIELD (See Instructions)

Gross Investment Income (Section 804(b))	1. Interest Received	2. Amount of Deduction	3. Balance (Col. 1 less Col. 2)	4. Mean of Beginning and End of Year Amounts
1. Interest on:				
(a) [illegible]	35,796.15	1,687.00	784.38	36,637.79
(b) [illegible]	0	0	0	0
(c) [illegible]	0	0	0	0
(d) [illegible]	46,445.34	25.00	11.00	46,459.34
(e) [illegible]	6,315.69	6,309.98	5,953.05	6,321.72
(f) [illegible]	973,457.47	5,982.98	6,749.41	974,669.74
2. Dividends on stock of:				
(a) Domestic corporations subject to taxation under Chapter 1, I.R.C.				0
(b) Certain preferred stock of public utilities taxable under Chapter 1, I.R.C.				0
(c) Foreign corporations				0
(d) Other corporations				0
3. Rents. (Attach schedule)				164,995.28
4. Royalties. (Attach schedule)				0
5. Leases, terminations, etc.				0
6. Gross income from trade or business other than investment business. (Attach schedule)				0
7. GROSS INVESTMENT INCOME (total lines 1-6)				1,139,662.02
Deductions (Section 804(c))				
8. Investment expenses. (Attach schedule) (See Schedule H)				104,602.57
9. Real estate expenses. (Attach schedule)				121,534.99
10. Depreciation. (Attach schedule)				19,249.85
11. Depletion of mines, oil and gas wells, timber, etc. (Attach schedule)				0
12. Trade or business deductions as provided in 804(c)(3) (Attach schedule)				0
13. Total deductions (lines 8-12)				245,387.41
14. INVESTMENT YIELD (line 7 less line 13)				894,277.61

SCHEDULE B—PART I—POLICY AND OTHER CONTRACT LIABILITY REQUIREMENTS (Sec. 805(a)) (See instructions)

1. Adjusted life insurance reserves (from Part V)	22,090,965.26	
2. Multiplied by the adjusted reserves rate (lesser of line 1 or 7, Part III)	3.253782 %	718,791.00
3. Interest paid (from Part VI)		42,352.47
4. Policy and other contract liability requirements (Total of lines 2 and 3)		761,143.28

PART II—ASSETS (Sec. 805(b)(4))

	1. Beginning of Taxable Year	2. End of Taxable Year	3. Mean of Beginning and End of Year Amounts
1. Real estate	1,025,538.20	1,042,261.22	1,033,999.71
2. Mortgages:			
(a) Without service fees	3,485,485.50	3,376,927.90	3,431,206.70
(b) With service fees	5,733,561.81	5,599,697.64	5,669,729.72
	275,700.00	272,700.00	274,200.00
3. Collateral loans	2,043,403.58	2,233,301.02	2,138,352.30
4. Policy loans, including premium notes	9,437,901.55	9,658,676.15	9,548,288.85
5. Corporate bonds	0	0	0
6. Stocks	1,713,602.00	2,402,436.00	2,058,019.00
7. Government obligations, etc. (Submit detailed schedule)	987,735.07	1,389,783.39	1,188,759.23
8. Bank deposits, cash, etc.	1,282,546.89	1,213,936.32	1,248,241.61
9. Other assets (Attach schedule)			
10. Totals	25,985,678.00	27,661,919.64	26,823,799.82

*Allowed under Section 805(a) (Attach schedule)

PART III—EARNINGS RATES (Sec. 805(b))

1. Current earnings rate (line 14, Schedule A divided by line 10, column 3, Part II)	3.333330
2. Earnings rate for first preceding year (Attach schedule)	3.[illegible]
3. Earnings rate for second preceding year (Attach schedule)	3.[illegible]
4. Earnings rate for third preceding year (Attach schedule)	3.[illegible]
5. Earnings rate for fourth preceding year (Attach schedule)	3.[illegible]
6. Total (lines 1-5)	16.[illegible]
7. Average earnings rate (See instructions)	3.253782

EXHIBIT 1

PART IV—AVERAGE INTEREST RATE (Section 805(b))

1. Name of Obligor	2. Interest Payment Dates	3. Int. Rate (Effective Rate)	4. Amount of Indebtedness	5. Amount of Discount or Premium	6. Other Consideration	7. Int. Rate
1. Life	Varies	Varies	20,548,850.00	20,786,550.00	267,700.00	693,959.28
2. Annuities	Varies	Varies	891,707.00	989,473.00	990.34	25,342.40
3. SGLIC	Varies	Varies	98,050.28	177,283.00	166,666.00	5,697.00
4. OSDAY	Varies	Varies	515,194.67	583,134.01	544,144.35	16,496.07
5. Totals					978,501.69	741,494.75

6. Average rate of interest computed in accordance with instructions (divide Column 7 total of column 5 divided by total of column 7) 3.40-25

* The interest for SGLIC and OSDAY is computed quarterly. Actual quarterly rates differ slightly.

PART V—ADJUSTED LIFE INSURANCE RESERVES (Sec. 805(b))

1. Items A of the reserves (col. 7, line 5, Part IV)		21,763,894.05
2. 1/ Multiplied by that percentage which equals	100%	
(a) Increased by 10 times the average rate of interest assumed (from line 6, Part IV)	134.04200	
(b) Total	32.51762	
(c) Reduced by 10 times the adjusted reserve rate (from line 2, Part I, Schedule D)		101,500.00
(d) Line (c) from line (b)		22,020,900.28
3. Adjusted life insurance reserves (line 1 multiplied by line 2(d))		

PART VI—INTEREST PAID (Sec. 805(b))

1. Interest on indebtedness	43,000.00
2. Amounts in the nature of interest	
3. Discount on purchased positions	
4. Total interest paid (lines 1-3)	

SCHEDULE C—TAXABLE INVESTMENT INCOME (See Instructions)

1. Policyholders' share (Sec. 804) (line 4, Part I, Sch. B) divided by line 14, Sch. A) but not to exceed 100%	85.33000	
2. Company's share		
3. Total		

	1. Total	2. Deferred Policyholders' share (line 3)	3. Company's share (line 2 - 1)
4. Interest wholly tax-exempt (line 11(a), column 4, Schedule A)	36,637.79	31,265.37	5,372.42
5. Interest partially tax-exempt (lines 11(b) and (d), column 4, Schedule A)	0	0	0
6. (a) Dividends from line 2(a), Schedule A	0	0	0
(b) Dividends from line 2(b), Schedule A	0	0	0
(c) Dividends from line 2(c), Schedule A	0	0	0
(d) Dividends from line 2(d), Schedule A	0	0	0
7. Other items of investment yield (line 14, Schedule A, less 4-6 above)	857,639.82	731,868.95	125,760.87
8. Total (Lines 4-7)	894,277.61	763,134.32	131,133.29

REDUCTIONS

9. Interest wholly tax-exempt (line 4, column 3)		5,372.42
10. Interest partially tax-exempt (25/52 of line 5, column 3)		
11. Dividends received deduct on:		
(a) 85% of dividends from line 6(a), column 3	0	
(b) 62.1135% of dividends from line 6(b), column 3	0	
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3	0	
(d) Total, but not to exceed 85% of taxable investment income (line 14, Schedule C) computed without regard to this deduction		0
12. Small business deduction (10% of line 14, Schedule A, not to exceed $25,000)		25,000.00
13. Total (lines 9, 10, 11(d) and 12)		30,372.42
14. Taxable investment income (line 8 less line 13, but not less than zero)		100,760.87

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EXHIBIT 1

1.—GAIN AND LOSS FROM OPERATIONS (See instructions)			
...holders' share (Sec. 809 (d)(5) Sch. I, Sch. I-1 divided by line 14, Sch. A) but not to exceed 100%			87.193...
...Company's share			12.806...
...	1. Total	2. Separate Accounts (Identify Titles on ...)	
...ed wholly tax exempt (line 1(a), column 4, Schedule A)	36,937.79	32,019.04	4,918.75
...ed partially tax exempt (lines 1(b) and (d), column 4, Schedule A)	0	0	0
...) Dividends from line 2(a), Schedule A	0	0	0
(d) Dividends from line 2(b), Schedule A	0	0	0
...) Dividends from line 2(c), Schedule A	0	0	0
...) Dividends from line 2(d), Schedule A	0	0	0
3. Other items of investment yield (line 14, Schedule A line 4-6 above)	657,619.82	749,521.28	106,118.54
4. Total (lines 1-3)	694,277.61	781,540.32	112,737.29
5. Gross premiums 6,319,787.11 Less: Return premiums etc. 151,066.25			6,168,720.86
6. (a) Decrease in reserves (after adjustment under 810(d)) (Attach schedule)			0
(b) Decrease in 811(b)(2) reserves (See line 3, Part IV, Schedule B-2)			0
11. Other amounts (Attach schedule)			552.22
12. Total (lines 5-11)			6,282,920.64
DEDUCTIONS			
13. Death benefits, etc.			3,612,465.00
14. Increase in reserves (after reduction for investment yield under 810(b)) (Attach schedule)			889,041.69
15. Assumption by another person of liabilities under insurance, etc., contracts			0
16. Interest wholly tax-exempt (line 4, column 3)			4,918.75
17. Interest partially tax-exempt (85/52 of line 5, column 3)			0
18. Investment expenses, etc., not deducted on Schedule A (Attach schedule)			10,183.63
19. Small business deduction (10 percent of line 14, Schedule A, not to exceed $25,000)			25,000.00
20. Other deductions not deducted on Schedule A (Attach schedule)			2,170,673.30
21. Total (lines 13-20)			5,712,282.37
22. Dividends received deduction (See instructions)			
(a) 85% of dividends received from line 6(a), column 3	0		
(b) 62.115% of dividends from line 6(b), column 3	0		
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3	0		
(d) Total, but not to exceed 85% of the excess, if any, of line 12 over line 21			0
23. Operations loss deduction (Attach schedule)			5,428,561.93
24. Tentative deduction (lines 21-23)			284,358.71
25. Plus: (a) Group life, accident, and health insurance (line 7, Part I, Schedule B-2)			284,358.71
(b) Certain nonparticipating contracts (line 8, Part I, Schedule B-2)			0
(c) Dividends to policyholders (line 11, Part I, Schedule B-2)			0
26. Total deductions (line 24 plus line 25)			284,358.71
27. Gain (loss) from operations (line 12 less line 26)			10,220.00

EXHIBIT 1

SCHEDULE D-6.—REQUIRED INTEREST (Sec. 809(d)(5))

Page 4

	1. Rate	2. Beginning of Taxable Year	3. End of Taxable Year	4. Mean (Columns 2 plus 3)	5. Column 4 (mean) multiplied by Column 1 (rate)
1. 809(d)(2) Reserves from line 2, column 6, Part IV, Schedule D					740,876.03
2. 809(d)(3) Reserves	Various	730,213.00	705,412.00	717,844.00	21,691.29
3. 809(d)(4) Reserves	Various	490,726.00	534,839.00	512,782.00	17,849.16
4. 809(d)(5) Reserves	Various	50,218.21	62,167.01	56,192.61	1,123.84
5. Required reduction (Total of lines 1—4)					781,540.32

SCHEDULE D-6.—PART I—LIMITATION ON LINE 22, SCHEDULE E DEDUCTION (Sec. 809(f))

1. Statutory amount		250,000
2. (a) From line 12, Schedule E	9,282,080.34	
(b) Less: Tentative deduction, line 24, Schedule E	8,492,565.34	
3. Gain from operations (offset copied to line 28, Schedule E	789,455.00	
4. Less: Taxable investment income (line 14, Schedule C)	100,760.87	688,694.13
5. Excess of line 3 over line 4 (but not less than zero)		938,694.13
6. Maximum possible deduction for line 22, Schedule E (line 1 plus line 5)		47,749.74
7. Deduction for group life, accident, and health insurance (Part II) (Not in excess of line 6)		890,944.39
8. Maximum deduction for certain nonparticipating contracts (line 6 less line 7)		127,116.96
9. Deduction for certain nonparticipating contracts (Part III) (Not in excess of line 8)		763,827.43
10. Maximum deduction for dividends to policyholders (line 8 less line 9)		453,368.22
11. Deduction for dividends to policyholders (Part IV) (Not in excess of line 10)		

PART II—GROUP LIFE, ACCIDENT, AND HEALTH INSURANCE (Sec. 809(d)(9))

1. Net premiums		2,387,487.15
2. Multiplied by		47,749.74
3. Tentative deduction		

PART III—CERTAIN NONPARTICIPATING CONTRACTS (Sec. 809(d)(10))

1. (a) Reserve at the end of the taxable year	20,550,115.02	
(b) Reserve at the beginning of the taxable year	19,278,945.38	
(c) Increase (if the difference is negative, enter "0")	1,271,169.64	
(d) Multiplied by	10%	127,116.96
2. (a) Net premiums	3,065,676.34	
(b) Multiplied by	3%	91,970.29
3. Tentative deduction—the greater of line 1 or line 2		127,116.96

PART IV—DIVIDENDS TO POLICYHOLDERS (Sec. 809(d)(5))

1. Dividends paid to policyholders		444,456.63
2. (a) Increased by the excess of (1) over (2):		
(1) Reserve as of the end of the taxable year	204,949.47	
(2) Reserve as of the end of the preceding taxable year	196,037.88	8,911.59
OR		
(b) Decreased by the excess of (1) over (2):		
(1) Reserve as of the end of the preceding taxable year		
(2) Reserve as of the end of the taxable year		
3. If positive, enter on line 11, Schedule D-2; if negative, enter on line 10(b), Schedule E		453,368.22

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EXHIBIT 1

Page 4a

1. Balance as of January 1, 1959			130,990.48
2. Life insurance company taxable income			0
3. Formerly tax-exempt interest deduction (Section 247 of Form 1120 and 164, column 4, Schedule A)			
4. Dividends received deduction:			
(a) 85% of dividends received from line 26(a), Schedule A		0	
(b) 82.115% of dividends received from line 26(b), Schedule A		0	
(c) 85% of dividends received from wholly foreign corporations		0	0
(d) Total. Not part to exceed 85% of line 12 less line 31, Schedule E			36,637.79
5. Interest wholly exempt less line 14(c), column 4, Schedule A)			25,000.00
6. Small business deduction (See 18, Schedule D			192,620.27
7. Total (Limit 1-6)			62,615.43
8. Less: Tax liability for 1959 (under 6258a)			130,013.22
9. Excess of line 7 over line 8			70,000.00
10. Less: Distributions in 1959 (Not to exceed line 9)			60,013.22
11. Balance as of December 31, 1959 (line 9 less line 10)			

SCHEDULE E.—LIMITATION OF INVESTMENT EXPENSE DEDUCTION (Schedule E need not be filled in if no deduction is claimed for any general expenses that are allocable to investment income.)

1. Mean of the assets for the taxable year (line 10, column 3, Part II, Schedule B)			26,021,798.62
2. One-fourth of 1% of the mean of the assets (line 1)			67,049.50
3. Mortgage service fees			28,965.05
4. The greater of (a) or (b):			
(a) (i) Investment yield computed without regard to investment expenses		1,147,641.26	
(ii) Three-and three-fourths percent of line 1		1,005,892.46	
(iii) Excess (line (i) over line (ii))		141,748.80	
(iv) One-fourth of line (iii)		35,437.20	
(v) Reduced by mortgage service fees from 3		28,965.05	
(vi) Line (v) less line (v)		6,472.15	
(b) One-fourth of 1% of the amount on line 2(a), column 3, Part II, Schedule B		8,578.02	8,578.02
5. Limit on deduction for investment expenses (Total lines 2-4)			104,602.57

K. Did you at any time during the taxable year own directly or indirectly 50% or more of the voting stock of a domestic corporation?
☐ Yes ☒ No

L. Did any corporation, individual, partnership, trust, or association at any time during the taxable year own directly or indirectly 50% or more of your voting stock?
☐ Yes ☒ No
If either answer is "Yes," see instruction N.

M. Did you at any time during the taxable year own directly or indirectly any stock of a foreign corporation? (If "Yes," attach statement required by General Instruction J.)
☐ Yes ☒ No

N. Did you file with the District Director a copy of the annual statement for the preceding year as required by General Instruction K?
☒ Yes ☐ No If "Yes," state office in which filed.
Oklahoma City, Oklahoma

O. If a copy of the annual statement does not accompany this return, state why the statement is not attached.
Filed with original return

EXHIBIT 1

c-1.

SCHEDULE G.—POLICYHOLDERS SURPLUS ACCOUNT (Sec. 815(a)) Page 4

1. Balance as of the beginning of the taxable year			
2. Add: (a) 50 percent of the excess, if any, of the gain from operations over the taxable investment income (line 2, page 1)		30,229.61	
(b) The deduction for certain computer-software contracts (line 25(a), Schedule D)		127,116.96	
(c) The deduction for group life, accident, and health insurance (line 25(c), Schedule D)		47,749.74	205,096.31
3. Total (line 1 plus line 2)			205,096.31
4. Less: (a) Actual distributions only to excess of line 10, Schedule F		0	
(b) Tax increase on 4(a) by reason of 809(b)(3)		0	
(c) Amounts treated as distributions (See instructions)		0	
(d) Tax increase on 4(c) by reason of 809(b)(3)		0	
(e) Subtractions required under 815(b)		0	0
5. Total of lines 4(a)–(d) (Not to exceed line 3) (Enter here and on line 3, page 1)			205,096.31
6. Balance as of the end of the year (line 3 less line 5)			

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EXHIBIT 1

IN THE UNITED STATES DISTRICT COURT

FORM 1120 L — U.S. LIFE INSURANCE COMPANY INCOME TAX RETURN — FOR CALENDAR YEAR 1958 — 2030

Do not write in space below

PLEASE TYPE OR PRINT PLAINLY

Plaintiff's Exhibit 7

The Atlas Life Insurance Company

415 South Boston Avenue, Tulsa 3, Oklahoma

September 25, 1918 — Oklahoma — 01-0513Z

35,485.55	Not applicable to this company	430,508.05

LIFE INSURANCE COMPANY TAXABLE INCOME

(a) The taxable investment income (Schedule C)	89,502.27	
(b) The gain (loss) from operations (Schedule D)	129,201.04	
(c) The smaller of (a) or (b)		89,502.27
50 percent of the excess, if any, of (b) over (a)		19,849.39
Life insurance company taxable income (Total lines 1(c) and 2)		109,351.66

COMPUTATION OF TAX DUE OR REFUND

If amount of line 3 is:		
(a) Not over $25,000— Enter 30 percent of line 3 (32 percent if a consolidated return)		
(b) Over $25,000— Enter 52 percent of line 3 (54 percent if a consolidated return)	56,862.86	51,362.86
Subtract $5,500, and enter difference	5,500.00	
Less: Credit allowed a domestic corporation for income taxes paid to a foreign country or United States possession (Submit Form 1118)		0
Total income tax (line 4 less line 5)		51,362.86
Credits for amounts paid on 1958 income tax:		
(a) Tax paid with application for extension of time in which to file	64,055.79	
(b) Payments and credit on 1958 Declaration of Estimated Tax		64,055.79
If tax (line 6) is larger than payments (line 7), the balance is TAX DUE. Enter such balance here		
If payments (line 7) are larger than tax (line 6) Enter the OVERPAYMENT here		12,692.93
Enter amount of line 9 you want: Credited on 1959 estimated tax		
Refunded	12,692.93	

SIGNATURE AND VERIFICATION (See Instruction E)

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and, to the best of my knowledge and belief is a true, correct, and complete return. If the return is prepared by a person other than the taxpayer, his declaration is based on all the information relating to the matters required to be reported in the return of which he has knowledge.

CORPORATE SEAL

(Date) (Signature of officer) (Title)

(Date) (Individual or firm signature) (Address)

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EXHIBIT 2 — PX 7. — FORM 1120 L—1958

Page 3

SCHEDULE A—INVESTMENT YIELD (See instructions)

Line no.	Gross Investment Income (Section 804(b))	1. Interest Received	2. Accrual of Discount	3. Amortization of Premium	4. Total (Use Col. 2 plus Col. 1 less Col. 3)
1.	Interest on:				
	(a) Bonds issued by obligors, except subsidiaries	(35,796.13)	(1,627.00)	(785.36)	(36,637.79)
	(b) Bonds issued by subsidiaries	0	0	0	0
	(c) Obligations guaranteed by the United States as to principal or interest	0	0	0	0
	(d) Other bonds (unless specifically exempt from tax)	46,445.34	25.00	11.00	46,459.34
	(e) Loans, notes, collateral loans, bank deposits, bonds, debentures, etc.	891,215.68	6,309.98	5,953.05	891,572.61
	Totals	937,661.02	6,334.98	5,964.05	938,031.95
2.	Dividends on stock of:				
	(a) Domestic corporations subject to taxation under Chapter 1, I.R.C.				0
	(b) Certain preferred stock of public utilities taxable under Chapter 1, I.R.C.				0
	(c) Foreign corporations				0
	(d) Other corporations				0
3.	Rents. (Attach schedule)				164,995.28
4.	Royalties. (Attach schedule)				0
5.	Leases, terminations, etc.				0
6.	Gross income from trade or business other than insurance business. (Attach schedule)				0
7.	GROSS INVESTMENT INCOME (total lines 1–6)				1,103,027.23
	Deductions (Section 804(d))				
8.	Investment expenses. (Attach schedule) (See Schedule H)				104,602.57
9.	Real estate expenses. (Attach schedule)				121,534.99
10.	Depreciation. (Attach schedule)				19,249.85
11.	Depletion of mines, oil and gas wells, timber, etc. (Attach schedule)				0
12.	Trade or business deductions as provided in 804(d)(2) (Attach schedule)				0
13.	Total deductions (lines 8–12)				245,387.41
14.	INVESTMENT YIELD (line 7 less line 13)				857,639.82

SCHEDULE B—PART I—POLICY AND OTHER CONTRACT LIABILITY REQUIREMENTS (Sec. 805(a)) (See instructions)

1.	Adjusted life insurance reserves (page Part V)	22,375,659.00
2.	Multiplied by the adjusted reserves rate (lesser of lines 1 or 7, Part III)	3.12297 %
3.	Interest paid (from Part V)	698,785.12
4.	Policy and other contract liability requirements (Total of lines 2 and 3)	44,352.43
		743,137.55

PART II—ASSETS (Sec. 805(b)(4))

		1. Beginning of Taxable Year	2. End of Taxable Year	3. Mean of columns 1 and column 2
1.	Real estate	1,025,738.20	1,042,261.22	1,033,999.71
2.	Mortgages:			
	(a) Without service fees	3,485,485.50	3,376,927.90	3,431,206.70
	(b) With service fees	5,733,561.81	5,599,897.64	5,666,729.72
3.	Collateral loans	275,700.00	272,700.00	274,200.00
4.	Policy loans, including premium notes	2,043,403.98	2,233,301.02	2,138,352.50
5.	Corporate bonds	9,437,901.55	9,656,676.15	9,547,288.85
6.	Stocks	0	0	0
7.	Government obligations, etc. (Submit detailed schedule)	1,713,602.00	2,902,436.00	2,308,019.00
8.	Bank deposits, cash, etc.	987,738.07	1,363,781.39	1,175,760.73
9.	Other assets (Attach schedule)	1,282,546.89	1,211,936.32	1,248,241.61
10.	Totals	25,985,678.00	27,661,919.64	26,823,798.82

Adjusted under Section 806(b) (Attach schedule)

PART III—EARNINGS RATES (Sec. 805(b))

1.	Current earnings rate (line 14, Schedule A divided by line 10, column 3, Part II)	3.19731 %
2.	Earnings rate for first preceding year (Attach schedule)	3.16190 %
3.	Earnings rate for second preceding year (Attach schedule)	3.08326 %
4.	Earnings rate for third preceding year (Attach schedule)	3.07247 %
5.	Earnings rate for fourth preceding year (Attach schedule)	3.03923 %
6.	Total (lines 1–5)	15.61485
7.	Average earnings rate (See instructions)	3.12297 %

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1. Description	2. Country of Issue	3. Rate of Interest	4. Amount of Reserve (Schedule D)	5. Amount of Policy Loans (Schedule C)	6. Mean of ends of year	7. Interest Earned (Schedule A)
a. Life	Various	Various	20,548,850.00	2,796,250.00	23,167,700.00	693,939.36
b. Annuities	Various	Various	881,797.00	988,471.00	929,090.34	25,342.48
c. Supplementary Contracts	Various	Various	98,099.00	177,883.43	137,666.86	4,697.52
d. Dividend Accumulations	Various	Various	515,194.67	581,194.03	582,144.35	16,876.67
e. Other					23,761,601.55	740,876.03
f. Total						3.40420%

g. Average rate of interest computed to consolidate life insurance reserves (total of column 6 divided by total of column 7)

*Use insurance for group and other subdivisions — *Interest rates differ through subdivision

PART V—ADJUSTED LIFE INSURANCE RESERVES (See Instructions)

1. Mean of the reserves (col. 7, line 6, Part IV)		21,761,601.55
2. (a) Multiplied by that percentage which equals	100%	
(b) Increased by 10 times the average rate of interest assumed (from line 6, Part IV)	35.05%	
(c) Total	134.04200	
(d) Reduced by 10 times the adjusted reserves rate (from line 2, Part I, Schedule B)	31.22970	
(e) Line (c) less line (d)		102.81230 %
3. Adjusted life insurance reserves (line 1 multiplied by line 2(e))		22,375,659.00

PART VI—INTEREST PAID (See Instructions)

1. Interest on indebtedness	0
2. Amounts in the nature of interest	41,094.36
3. Discount on prepaid premiums	1,258.07
4. Total (interest paid (lines 1-3)	44,352.43

SCHEDULE G—TAXABLE INVESTMENT INCOME (See Instructions)

1. Policyholders' share (Sec. 804) (line 4, Part I, Sch. B divided by line 14, Sch. A) but not to exceed 100%			86.6491 %
2. Company's share			13.3509 %
3. Total			100.00 %

	1. Total	2. Deducted Policyholders' share (line 1 times col. 1)	3. Company's share (line 1 less col. 2)
	** EXCLUDED **		
4. Interest wholly tax-exempt (line 11(a), column 4, Schedule A)			
5. Interest partially tax-exempt (lines 10(a) and (c), column 4, Schedule A)			
6. (a) Dividends from line 2(a), Schedule A			
(b) Dividends from line 2(b), Schedule A			
(c) Dividends from line 2(c), Schedule A	0		
(d) Dividends from line 2(d), Schedule A	857,639.82	743,137.55	114,502.27
7. Other items of investment yield (line 14, Schedule A, less 4-6 above)	857,639.82	743,137.55	114,502.27
8. Total (Lines 4-7)			0
REDUCTIONS			0
9. Interest wholly tax-exempt (line 4, column 3)			
10. Interest partially tax-exempt (30/52 of line 5, column 3)			
11. Dividends received deduction:			
(a) 85% of dividends from line 6(a), column 3	0		
(b) 63.1115% of dividends from line 6(b), column 3	0		
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3	0		
(d) Total, but not to exceed 85% of taxable investment income (line 14, Schedule C) computed without regard to this deduction			0
12. Small business deduction (10% of line 14, Schedule A, not to exceed $25,000)			25,000.00
13. Total (lines 9, 10, 11(d), and 12)			25,000.00
14. Taxable investment income (line 8 less line 13, but not less than zero)			89,502.27

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EXHIBIT 2

	1. Total	2. Exclusive Participating Shareholders' Policyholders'	3. Company's share (Line 2 times Sch. C)
	** EXCLUDED **		
1. Policyholders' share (Sec. 8C (Line 3, Sec. E-1 divided by line 14, Sch. A), but not to exceed 10			
2. Company's share			
3. Total			
4. Interest wholly tax-exempt (line 1(a), column 4, Schedule A)			
5. Interest partially tax-exempt (lines 1(b) and (d), column 4, Schedule A)			
6. (a) Dividends from line 2(a), Schedule A			
(b) Dividends from line 2(b), Schedule A			
(c) Dividends from line 2(c), Schedule A			
(d) Dividends from line 2(d), Schedule A			
7. Other items of investment yield (line 14, Schedule A less 4-6 above)	857,639.82	781,540.32	76,099.50
8. Total (lines 4-7)	857,639.82	781,540.32	76,099.50
9. Gross premiums 6,319,787.11 Less: Return premiums, etc. 151,066.28			6,168,720.83
10. (a) Decrease in reserves (after adjustment under 810(d)) (Attach schedule)			
(b) Decrease in 811(b)(2) reserves (See line 3, Part IV, Schedule E-2)			662.22
11. Other amounts (Attach schedule)			6,245,382.55
12. Total (lines 8-11)			3,622,463.01
DEDUCTIONS			669,682.65
13. Death benefits, etc.			0
14. Increase in reserves (after reduction for investment yield under 810(d)) (Attach schedule)			0
15. Annuities by another person of liabilities under insurance, etc., contracts			0
16. Annuities wholly tax-exempt (line 4, column 3)			10,193.03
17. Interest partially tax-exempt (3%) of line 5, column 3)			25,000.00
18. Investment expenses, etc., not deducted on Schedule A (Attach schedule)			1,170.57
19. Small business deduction (10 percent of line 14, Schedule A, not to exceed $25,000)			5,487,946.59
20. Other deductions not deducted on Schedule A (Attach schedule)			
21. Total (lines 13-20)			
22. Dividends received deduction (See instructions)			
(a) 85% of dividends received from line 6(a), column 3	0		
(b) 62.115% of dividends from line 6(b), column 3	0		
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3	0		
(d) Total, but not to exceed 85% of line 21			
23. Operations loss deduction (Attach schedule)			
24. Insurance deduction (lines 21-23)			
25. Plus: (a) Group life, accident, and he (Schedule E-2)			
(b) Certain nonparticipating ac (line 6-2)			
(c) Dividends to policyholders f			
26. Total deductions (line 24 plus			
27. Gain from operations (line 12 less line 26)			

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SCHEDULE D-1.—REQUIRED INTEREST [illegible] 809(a)(2))

	1. Rate	2. Beginning of Taxable Year	3. End of Taxable Year	4. Mean (Columns 2 plus 3)	5. Column 1 times column 4
1. 810(a)(1) Reserves (from line 5, column 8, Part IV, Schedule B)					740,676.03
2. 810(a)(3) Reserves	Various	730,213.00	705,412.00	717,844.00	21,691.29
3. 810(a)(4) Reserves	Various	490,726.00	524,839.00	512,782.00	17,849.16
4. 810(a)(5) Reserves	Various	50,218.21	62,167.01	56,192.61	1,123.84
5. Required interest (Total, lines 1-4)					781,540.32

SCHEDULE D-2.—PART I—LIMITATION ON LINE 25, SCHEDULE E DEDUCTION (Sec. 809(f))

1. Statutory amount			250,000
2. (a) From line 12, Schedule E	6,245,382.55		
(b) Less: Tentative deduction, line 24, Schedule E	5,487,946.59		
3. Gain from operations without regard to line 25, Schedule E	757,435.96		
4. Less: Taxable investment income (line 14, Schedule C)	89,502.27		667,933.69
5. Excess of line 3 over line 4 (but not less than zero)			917,933.69
6. Maximum possible deduction for line 25, Schedule E (line 1 plus line 5)			47,749.74
7. Deduction for group life, accident, and health insurance (Part II) (Not in excess of line 6)			870,183.95
8. Maximum deduction for certain nonparticipating contracts (line 6 less line 7)			127,116.96
9. Deduction for certain nonparticipating contracts (Part III) (Not in excess of line 8)			343,066.99
10. Maximum deduction for dividends to policyholders (line 8 less line 9)			453,368.22
11. Deduction for dividends to policyholders (Part IV) (Not in excess of line 10)			

PART II—GROUP LIFE, ACCIDENT, AND HEALTH INSURANCE (Sec. 809(d)(6))

1. Net premiums			2,387,487.15
2. Multiplied by			2%
3. Tentative deduction			47,749.74

PART III—CERTAIN NONPARTICIPATING CONTRACTS (Sec. 809(d)(5))

1. (a) Reserve at the end of the taxable year	20,550,115.02		
(b) Reserve at the beginning of the taxable year	19,278,945.36		
(c) Increase (if the difference is negative, enter "0")	1,271,169.66		
(d) Multiplied by	10%		127,116.96
2. (a) Net premiums	3,065,676.34		
(b) Multiplied by	3%		91,970.29
3. Tentative deduction—the greater of line 1 or line 2			127,116.96

PART IV—DIVIDENDS TO POLICYHOLDERS (Sec. 809(d)(3))

1. Dividends paid to policyholders			444,456.63
2. (a) Increased by the excess of (1) over (2):			
(1) Reserve as of the end of the taxable year	204,949.47		8,911.59
(2) Reserve as of the end of the preceding taxable year	196,037.88		
OR			
(b) Decreased by the excess of (1) over (2):			
(1) Reserve as of the end of the preceding taxable year			
(2) Reserve as of the end of the taxable year			453,368.22
3. If positive, enter on line 11, Schedule E-2; if negative, enter on line 10(b), Schedule E			

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EXHIBIT 2

SCHEDULE F.—SHAREHOLDERS SURPLUS ACCOUNT (Sec. 815(b))

Page 4a

1. Balance as of January 1, 1958			zero 109,351.66
2. Life insurance company taxable income			0
3. Partially tax-exempt interest deduction (20/52 of item 10(a) and (c), column 4, Schedule A)			
4. Dividends received deduction:			
(a) 85% of dividends received from line 21(a), Schedule A		0	
(b) 62.115% of dividends received from line 21(b), Schedule A		0	
(c) 85% of dividends received from certain foreign corporations		0	
(d) Total, but not to exceed 85% of line 12 less line 21, Schedule E			0
5. Interest wholly exempt from tax (line 11(a), column 4, Schedule A)			36,637.79
6. Small business deduction (line 19, Schedule D)			25,000.00
7. Total (lines 1–6)			170,989.45
8. Less Tax Liability for 1958 under 802(a)			54,362.86
9. Excess of line 7 over line 8			119,626.59
10. Less Distributions in 1959 (But to exceed line 9)			70,000.00
11. Balance as of December 31, 1959 (line 9 less line 10)			49,626.59

SCHEDULE H.—LIMITATION OF INVESTMENT EXPENSE DEDUCTION (Schedule H need not be filed as if no deduction is claimed for any general expenses that are allocated to investment income.)

1. Means of the assets for the taxable year (line 10, column 3, Part II, Schedule B)		26,823,798.82
2. One-fourth of 1% of the means of the assets (line 1)		67,059.50
3. Mortgage service fees		28,965.05
4. The greater of (a) or (b):		
(a) (i) Investment yield computed without regard to investment expenses	1,147,641.26	
(ii) Three and three-fourths percent of line 1	1,005,892.46	
(iii) Excess (line (i) over line (ii))	141,748.80	
(b) One-fourth of line (a)(ii)	35,437.20	
(c) Reduced by mortgage service fees (line 3)	28,965.05	
(d) Less (c) (not less than (b))	6,472.15	
(e) One-fourth of 1% of the amount on line 2(a), column 2, Part II, Schedule B	8,578.02	8,578.02
5. Limit on deduction for investment expenses (Total lines 2–4)		104,602.57

M. Did you file with the ...rict Director a copy of the annual statement for the preceding year as required by General Instruction K?
☒ Yes ☐ No If "Yes," state office in which filed.
Oklahoma City, Oklahoma

N. Did you, at any time during the taxable year, own directly or indirectly 50% or more of the voting stock of a domestic corporation?
☐ Yes ☒ No

O. If a copy of the annual statement does not accompany this return, state why the statement is not attached.
Filed with original return

P. Did any corporation, individual, partnership, trust, or association at any time during the taxable year own directly or indirectly 50% or more of your voting stock?
☐ Yes ☒ No
If answer is "Yes," see instruction N.

Q. Did you at any time during the taxable year own directly or indirectly any stock of a foreign corporation? (If "Yes," attach statement required by General Instruction I.)
☐ Yes ☒ No

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EXHIBIT 2

SCHEDULE G.—POLICYHOLDERS SURPLUS ACCOUNT (Sec. 815(a))

			Page 4b amo
1. Balance as of the beginning of the taxable year			
2. Add: (a) 50 percent of the excess, if any, of the gain from operations over the taxable investment income (line 2, page 1)		19,609.39 127,116.96	
(b) The deduction for certain nonparticipating contracts (line 25(b), Schedule D)			
(c) The deduction for group life, accident, and health insurance (line 25(a), Schedule D)		47,749.74	194,716.09
3. Total (line 1 plus line 2)			194,716.09
4. Less: (a) Actual distributions only to excess of line 10, Schedule F	0		
(b) Tax increase on 4(a) by reason of 802(b)(3)	0		
(c) Amounts treated as distributions (See instructions)	0		
(d) Tax increase on 4(c) by reason of 802(b)(3)	0		
(e) Subtractions required under 815(d)	0		
5. Total of lines 4(a) - (d) (Not to exceed line 3) (Enter here and on line 3, page 1)			0
6. Balance as of the end of the year (line 3 less line 5)			194,716.09

EXHIBIT 2

IN UNITED STATES DISTRICT COURT

Pg 1

Form 1120 L — U.S. LIFE INSURANCE COMPANY INCOME TAX RETURN FOR CALENDAR YEAR 1958 — 1958

Do not write in space below

PLEASE TYPE OR PRINT PLAINLY

Plaintiff's Exhibit 9

Name: The Atlas Life Insurance Company

Address: 415 South Boston Avenue, Tulsa 3, Oklahoma

a. Date and place incorporated: September 25, 1918 Oklahoma

b. Employer's identification number: 01-05132

c. Amount of total dependable income: 430,508.05

d. Amount of total dependable income claimed for current year: 35,405.55

e. Amount of total investment deductions as defined in Sec. 804(a)(2): Not applicable to this company.

f. Is this a consolidated return? (If "Yes," see Instruction 5L) ☐ Yes ☒ No

g. Do you have any subsidiary essentially noninsurance? (If "Yes," see Instruction 5M) ☐ Yes ☒ No

h. Are you a mutual or mutual benefit insurance company, or mutual marine, to the computation of taxable income under section 821(a)(2)? (If "Yes," see Instruction 5N) ☐ Yes ☒ No

i. Did you file Forms 1096 and 1099 for the calendar year in connection with taxable dividends? (See Statement of Information 5L) ☒ Yes ☐ No

j. Did you file Forms 1096 and 1099 for the calendar year in connection with other payments? (See Statement of Information 5L) ☒ Yes ☐ No

☐ Yes ☒ No

LIFE INSURANCE COMPANY TAXABLE INCOME

1. (a) The taxable investment income (Schedule C)	950	101,190.77	101,190.77	950
(b) The gain from operations (Schedule D)	954	162,184.34	30,496.79	407
(c) The smaller of (a) or (b)				
2. 50 percent of the excess, if any, of 1(a) over 1(c)			131,687.56	957
3. Life insurance company taxable income (Total lines 1(c) and 2)				

COMPUTATION OF TAX DUE OR REFUND

4. If amount of line 3 is: (a) Not over $25,000— Enter 30 percent of line 3 (22 percent if a consolidated return)				
(b) Over $25,000— Enter $7,500 and 52 percent of line 3 (34 percent if a consolidated return) Subtract $25,000 and enter difference	964	68,477.53 / 8,500.00	62,977.53	964
5. Less: Credit allowed a domestic corporation for income taxes paid to a foreign country or United States possession (Submit Form 1118)			0	
6. Total income tax (line 4 less line 5)			62,977.53	966
7. Credits for amounts paid on 1958 income tax: (a) Tax paid with applications for extension of time to file		64,055.79	64,055.79	
(b) Payments and credits on 1958 Declaration of Estimated Tax				
8. If tax (line 6) is larger than payments (line 7), the balance is TAX DUE. Enter such balance here →			1,078.26	968
9. If payments (line 7) are larger than tax (line 6) Enter the OVERPAYMENT here →				
10. Enter amount of line 9 you want Credited on 1959 estimated tax				
Refunded		1,078.26	968	

SIGNATURE AND VERIFICATION (See Instruction E)

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me and to the best of my knowledge and belief is a true, correct, and complete return. If the return is prepared by a person other than the taxpayer, his declaration is based on all the information relating to the matters required to be reported in the return of which he has knowledge.

CORPORATE SEAL

(Date) (Signature of officer) (Title)

(Date) (Individual or firm signature) (Address)

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EXHIBIT 1-T.

PX 9

FORM 1120 L—1958

p2

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SCHEDULE A.—INVESTMENT YIELD (See Instructions)

Line and Schedule No.	Gross Investment Income (Section 804(b))	1. Interest Earned	2. Accrual of Discount	3. Amortization of Premium	4. Total (In the Case of Lines 1 thru Columns 1 plus Columns 2 plus Columns 3)
1.	Interest on:	35,796.15	1,627.00	786.36	36,637.79
	(a) Wholly exempt obligations. (Attach schedule)	0	0	0	0
	(b) United States Savings Bonds and Treasury Bonds owned in excess of the aggregate limit of $5,000 owned prior to March 1, 1941	0	0	0	0
	(c) Obligations issued on or after March 1, 1941, by the United States or any agency or instrumentality thereof. (Attach schedule)	46,445.34	25.00	11.00	46,459.34
	(d) Other	892,215.66	6,309.98	2,953.05	892,572.61 /SSB
	Totals	974,457.17	7,961.98	6,749.41	975,669.74 /SSB
2.	Dividends on stock of:				0
	(a) Domestic corporations subject to taxation under Chapter 1, I.R.C.				0
	(b) Certain preferred stock of public utilities taxable under Chapter 1, I.R.C.				0
	(c) Foreign corporations				0
	(d) Other corporations				164,995.28
3.	Rents. (Attach schedule)				0
4.	Royalties. (Attach schedule)				0
5.	Leases, terminations, etc.				0
6.	Gross income from trade or business other than insurance business. (Attach schedule)				1,140,665.02 /SSB
7.	GROSS INVESTMENT INCOME (total lines 1-6)				
	Deductions (Section 804(a))				
8.	Investment expenses. (Attach schedule) (See Schedule H)				104,602.57
9.	Real estate expenses. (Attach schedule)				121,534.99
10.	Depreciation. (Attach schedule)				19,249.85
11.	Depletion of mines, oil and gas wells, timber, etc. (Attach schedule)				0
12.	Trade or business deductions as provided in 804(a)(3) (Attach schedule)				0
13.	Total deductions (lines 8-12)				245,387.41
14.	INVESTMENT YIELD (line 7 less line 13)				895,277.61 /SSB

SCHEDULE B.—PART I—POLICY AND OTHER CONTRACT LIABILITY REQUIREMENTS (Sec. 806(a)) (See Instructions.)

1. Adjusted life insurance reserves (from Part V)	2.096	22,082,869.23	719,349.91 SSB
2. Multiplied by the adjusted reserves rate (Lesser of lines 1 or 7, Part III)	.032740	3.257502%	4,352.43
3. Interest paid (from Part VI)			76,702.34 SSB
4. Policy and other contract liability requirements (Total of lines 2 and 3)			

PART II—ASSETS (Sec. 806(b)(4))

	1. Beginning of Taxable Year	2. End of Taxable Year	3. Mean of columns 1 and column 2
1. Real estate	1,025,738.20	1,042,261.22	1,033,999.71
2. Mortgages			
(a) Without service fees	3,485,485.50	3,376,927.90	3,431,206.70
(b) With service fees	5,733,561.81	5,599,897.64	5,666,729.72
3. Collateral loans	275,700.00	272,700.00	274,200.00
4. Policy loans, including premium notes	2,043,403.98	2,233,301.02	2,138,352.50
5. Corporate bonds	9,437,901.55	9,656,679.15	9,547,288.85
6. Stocks	0	0	0
7. Government obligations, etc. (Submit detailed schedule)	1,713,602.00	2,902,436.00	2,308,019.00
8. Bank deposits, cash, etc.	987,738.07	1,363,783.39	1,175,760.73
9. Other assets (Attach schedule)	1,282,546.89	1,213,930.32	1,248,241.61
10. Totals	25,985,678.00	27,661,919.64	26,823,798.82

*Adjusted under Section 806(b)(4) (Attach schedule)

PART III—EARNINGS RATES (Sec. 806(b))

1. Current earnings rate (line 14, Schedule A divided by line 10, column 3, Part II)	.033762	3.33762
2. Earnings rate for first preceding year (Attach schedule)	.031406	3.31406
3. Earnings rate for second preceding year (Attach schedule)	.032416	3.20416
4. Earnings rate for third preceding year (Attach schedule)	.032210	3.22957
5. Earnings rate for fourth preceding year (Attach schedule)	.032957	16.28754
6. Total (lines 1-5)	.162754	3.257502
7. Average earnings rate (See Instructions)	.032740	

EXHIBIT 1-T

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PART IV—AVERAGE INTEREST RATE ASSUMED (Sec. 809(d)(2))

1. Nature of Reserve (Life, Annuity, etc.)	2. Assumed Mortality or Morbidity Table	3. Assumed Interest Rate	4. Method of Computation (Reserve Bases, etc.)	5. Amount of Reserve at Beginning of Taxable Year	6. Amount of Reserve at End of Taxable Year	7. Mean of Columns 5 and 6	8. Column 7 times Column 3
1. Life	V a r i o u s			19,548,850.00	20,786,550.00	20,167,700.00	693,959.36
2. Annuities	V a r i o u s			893,707.00	984,473.68	939,090.34	25,342.48
3. SCLIC	V a r i o u s			98,050.26	177,283.43	137,666.86	4,697.52
4. Other	V a r i o u s			515,154.61	583,134.01	549,144.35	16,876.67
5. Totals						21,793,601.55	740,876.03

6. Average rate of interest assumed in computing life insurance reserves (total of column 8 divided by total of column 7) ..... 3.40420 %

*Adjusted under 809(d) (5) with subsidiary

**See instructions for 809(d) and (f) adjustments

PART V—ADJUSTED LIFE INSURANCE RESERVES (Sec. 809(d)(1))

1. Mean of the reserves (col. 7, line 6, Part IV)		21,761,601.55
2. (a) Multiplied by that percentage which equals	100%	
(b) Increased by 10 times the average rate of interest assumed (from line 6, Part IV)	10.0342	
(c) Total	134.0342	
(d) Reduced by 10 times the adjusted reserve rate (from line 2, Part I, Schedule H) .04440	32.5702	101.46698 %
(e) Line (d) less line (d)	.04440	22,082,869.23
3. Adjusted life insurance reserves (col. 1 multiplied by line 2(e))		

PART VI—INTEREST PAID (Sec. 809(d))

1. Interest on indebtedness	0
2. Amounts in the nature of interest	43,094.46
3. Discount on prepaid premiums	1,258.97
4. Total interest paid (lines 1-3)	44,352.43

SCHEDULE C—TAXABLE INVESTMENT INCOME (See Instructions)

1. Policyholders' share (Sec. 809) (line 4, Part I, Sch. B divided by line 14, Sch. A) but not to exceed 100% .84437		85.30341 %
2. Company's share .84437		14.69659 %
3. Total	100	%

	1. Total	2. Policyholders' share (line 1 times col. 1)	3. Company's share (line 1 times col. 1)
4. Interest wholly tax-exempt (line 11(a), column 4, Schedule A)	36,637.79	31,253.28	5,384.51
5. Interest partially tax-exempt (lines 10(a) and (d), column 4, Schedule A)	0	0	0
6. (a) Dividends from line 2(d), Schedule A	0	0	0
(b) Dividends from line 2(e), Schedule A	0	0	0
(c) Dividends from line 2(f), Schedule A	0	0	0
(d) Dividends from line 3(d), Schedule A	0	0	0
7. Other items of investment yield (line 14, Schedule A, lines 4-6 above)	858,639.82	732,449.05	126,190.77
8. Total (Lines 4-7)	895,277.61	763,702.33	131,575.28
REDUCTIONS			
9. Interest wholly tax-exempt (line 4, column 3)			5,384.51
10. Interest partially tax-exempt (85/85 of line 5, column 3)			0
11. Dividends received deductions:			
(a) 85% of dividends from line 6(a), column 3	0		
(b) 62.1115% of dividends from line 6(b), column 3	0		
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3	0		
(d) Total, but not to exceed 85% of taxable investment income (line 14, Schedule C) computed without regard to this deduction			0
12. Small business deduction (10% of line 14, Schedule A, not to exceed $25,000)			25,000.00
13. Total (lines 9, 10, 11(d), and 12)			30,384.51
14. Taxable investment income (line 8 less line 13, but not less than zero)			101,190.77

EXHIBIT 1-T

SCHEDULE E—GAIN AND LOSS FROM OPERATIONS (See Instructions)

1. Policyholders' share (Sec. 809) (Line X, Sch. K-1 divided by line 14, Sch. A), but not to exceed 100%			87.29586 %
2. Company's share			12.70414 %
3. Total			100 %
	1. Total	2. Exclusive Policyholders' share (Line 1 minus col. 3)	3. Company's share (Line 1 minus col. 2)
4. Interest wholly tax-exempt (line 1(a), column 4, Schedule A)	36,637.79	31,983.27	4,654.52
5. Interest partially tax-exempt (lines 1(b) and (d), column 4, Schedule A)	0	0	0
6. (a) Dividends from line 2(a), Schedule A	0	0	0
(b) Dividends from line 2(b), Schedule A	0	0	0
(c) Dividends from line 2(c), Schedule A	0	0	0
(d) Dividends from line 2(d), Schedule A	0	0	0
7. Other items of investment yield (line 14, Schedule A less 4-6 above)	858,639.82	749,557.02	109,082.80
8. Total (lines 4-7)	895,277.61	781,540.29	113,737.32
9. Gross premiums 6,319,787.11 Less Return premiums, etc. 151,086.28			6,168,700.83
10. (a) Decrease in reserves (after adjustment under §810(d)) (Attach schedule)			0
(b) Decrease in §810(c)(2) reserves (See line 2, Part IV, Schedule E-2)			0
11. Other accounts (Attach schedule)			582.22
12. Total (lines 9-11)			6,283,020.37
DEDUCTIONS			
13. Death benefits, etc.			3,612,468.01
14. Increase in reserves (after reduction for investment yield under §810(d)) (Attach schedule)			669,621.65
15. Assumption by another person of liabilities under insurance, etc., contracts			0
16. Interest wholly tax-exempt (line 4, column 3)			4,654.52
17. Interest partially tax-exempt (85/85 of line 5, column 3)			0
18. Interest paid or accrued on indebtedness (Attach schedule)			10,183.03
19. Investment expenses, etc., not deducted on Schedule A (Attach schedule)			25,000.00
20. Small business deduction (10 percent of line 14, Schedule A, not to exceed $25,000)			1,170,673.90
21. Other deductions not deducted on Schedule A (Attach schedule)			5,492,601.11
22. Total (lines 13-20)			
23. Dividends received deduction (See instructions):			
(a) 85% of dividends received (line 6(a), column 3)	0		
(b) 42.1175% of dividends received (line 6(b), column 3)	0		
(c) 85% of dividends from certain foreign corporations (line 6(c), column 3)	0		
(d) Total, but not to exceed 85% of the amount, if any, of line 12 over line 21			0
24. Operations loss deduction (Attach schedule)			0
25. Tentative deduction (lines 21-23)			5,492,601.11
26. Total (a) Group life, accident, and health insurance (line 7, Part I, Schedule E-2)			47,749.74
(b) Certain nonparticipating contracts (line 9, Part I, Schedule E-2)			127,116.56
(c) Dividends to policyholders (line 11, Part I, Schedule E-2)			453,368.22
(d) Total deductions (line 24 plus line 25)			6,120,836.03
27. Gain from operations (line 12 less line 26)			162,184.34

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SCHEDULE S-1.—REQUIRED INTEREST (Sec. 809(a)(2))

	1. Rate	2. Beginning of Taxable Year	3. End of Taxable Year	4. Mean (Column 2 plus 3)	5. Column 1 times column 4
1. 810(d)(1) Reserves from line 3, column 8, Part IV, Schedule B					740,876.03
2. 810(d)(2) Reserves	Various	730,213.00	705,412.00	717,844.00	21,691.29
3. 810(d)(4) Reserves	Various	490,726.00	534,839.00	512,782.00	17,849.16
4. 810(d)(5) Reserves	Various	50,218.21	62,167.01	56,192.61	1,123.84
5. Required interest (Total, lines 1-4)					781,540.32

SCHEDULE S-2.—PART I—LIMITATION ON LINE 33, SCHEDULE E DEDUCTION (Sec. 809(c))

1. Statutory amount			250 000
2. (a) From line 12, Schedule E	AAC	6,283,020.37	
(b) Less: Tentative deduction, line 34, Schedule E	AK	5,492,601.11	
3. Gain from operations without regard to line 25, Schedule E	TAX	790,419.26	
4. Less: Taxable investment income (line 14, Schedule C)	SUB	101,190.77	689,228.49 SUB
5. Excess of line 3 over line 4 (but not less than zero)			939,228.49 SUB
6. Maximum possible deduction for line 25, Schedule E (line 1 plus line 5)			47,749.74
7. Deduction for group life, accident, and health insurance (Part II) (Not in excess of line 6)			891,478.75 SUB
8. Maximum deduction for certain nonparticipating contracts (line 6 less line 7)			127,116.96
9. Deduction for certain nonparticipating contracts (Part III) (Not in excess of line 8)			764,361.79 SUB
10. Maximum deduction for dividends to policyholders (line 9 less line 9)			453,368.22
11. Deduction for dividends to policyholders (Part IV) (Not in excess of line 10)			

PART II—GROUP LIFE, ACCIDENT, AND HEALTH INSURANCE (Sec. 809(d)(8))

1. Net premiums		2,387,487.15
2. Multiplied by		2%
3. Tentative deduction		47,749.74

PART III—CERTAIN NONPARTICIPATING CONTRACTS (Sec. 809(d)(5))

1. (a) Reserve at the end of the taxable year		20,550,115.02	
(b) Reserve at the beginning of the taxable year		19,278,945.38	
(c) Increase (If the difference is negative, enter "0")		1,271,169.64	
(d) Multiplied by		10%	127,116.96
2. (a) Net premiums		3,065,676.34	
(b) Multiplied by		3%	91,970.29
3. Tentative deduction—the greater of line 1 or line 2			127,116.96

PART IV—DIVIDENDS TO POLICYHOLDERS (Sec. 809(d)(3))

1. Dividends paid to policyholders			444,456.63
2. (a) Increased by the excess of (1) over (2):			
(1) Reserve as of the end of the taxable year		204,949.47	
(2) Reserve as of the end of the preceding taxable year		196,037.88	8,911.59
OR			
(b) Decreased by the excess of (2) over (2):			
(1) Reserve as of the end of the preceding taxable year			
(2) Reserve as of the end of the taxable year			
3. If positive, enter on line 11, Schedule S-2; if negative, enter on line 10(b), Schedule E			453,368.22

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SCHEDULE F.—SHAREHOLDERS SURPLUS ACCOUNT (Sec. 815(b))

Page 4a

1. Balance as of January 1, 1958			31,687.56
2. Life insurance company taxable income			0
3. Partially tax-exempt interest deduction (2)(B) of lines 1(b) and (c), column 4, Schedule A)			
4. Dividends received deduction:			
(a) 85% of dividends received from line 2(a), Schedule A		0	
(b) 62.115% of dividends received from line 2(b), Schedule A		0	
(c) 85% of dividends received from certain foreign corporations		0	
(d) Total, but not to exceed 85% of line 12 less line 21, Schedule E			0
5. Interest wholly exempt from tax (line 1(c), column 4, Schedule A)			36,637.79
6. Small business deduction (line 19, Schedule D)			25,000.00
7. Total (lines 1-6)			193,325.35
8. Less: Tax liability for 1958 under 802(a)			62,977.53
9. Excess of line 7 over line 8			130,347.82
10. Less: Distributions in 1958 (not to exceed line 9)			70,000.00
11. Balance as of December 31, 1958 (line 9 less line 10)			60,347.82

SCHEDULE H.—LIMITATION OF INVESTMENT EXPENSE DEDUCTION (Schedule H need not be filed in if no deduction is claimed or any interest expenses that are allocated to investment income.)

1. Mean of the assets for the taxable year (line 10, column 3, Part II, Schedule B)			26,831,799.82
2. One-fourth of 1% of the mean of the assets (line 1)			67,059.50
3. Mortgage service fees			28,965.05
4. The greater of (a) or (b):			
(a) If investment yield computed without regard to investment expenses	1666	1,148,641.26	
(1) Three and three-fourths percent of line 1	1666	1,005,892.48	
(2) Excess (line (1) over line (a))		142,748.80	
(3) One-fourth of line (2)		35,687.20	
(4) Reduced by mortgage service fees (line 3)	446	28,965.05	
(5) Line (4) less line (4)		6,722.15	
(b) One-fourth of 1% of the amount on line 2(a), column 3, Part II, Schedule B		8,578.02	8,578.02
5. Limit on deduction for investment expenses (Total lines 2-4)			104,602.57

6. Did you, at any time during the taxable year own, directly or indirectly 50% or more of the voting stock of a domestic corporation?
☐ Yes ☒ No

7(a) Any corporation, individual, partnership, trust, or association at any time during the taxable year, own directly or indirectly 50% or more of your voting stock?
☐ Yes ☒ No
If either answer is "Yes," see Instruction H.

(b) Did you at any time during the taxable year own directly or indirectly any stock of a foreign corporation? If "Yes," attach statement required by General Instruction I.)
☐ Yes ☒ No

8. Did you file with the District Director a copy of the annual statement for the preceding year as required by General Instruction K?
☒ Yes ☐ No If "Yes," state office in which filed.
Oklahoma City, Oklahoma

9. If a copy of the annual statement does not accompany this return, state why the statement is not attached.
Filed with original return

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SCHEDULE G.—POLICYHOLDERS SURPLUS ACCOUNT (Sec. 815(a)) Page 4b

			zero
1. Balance as of the beginning of the taxable year			
2. Add: (a) 50 percent of the excess, if any, of the gain from operations over the taxable investment income (line 2, page 1)	30,496.79		
	127,116.96		
(b) The deduction for certain nonparticipating contracts (line 25(a), Schedule D)	47,749.74		205,363.49 407
(c) The deduction for group life, accident, and health insurance (line 25(c), Schedule D)			205,363.49 407
3. Total (line 1 plus line 2)			205,363.49 407
4. Less: (a) Actual distributions only in excess of line 10, Schedule F		0	
(b) Tax increase on 4(a) by reason of 802(b)(3)		0	
(c) Amounts treated as distributions (See instructions)		0	
(d) Tax increase on 4(c) by reason of 802(b)(3)		0	
(e) Subtractions required under 815(d)		0	
5. Total of lines 4(a)-(d) (Not to exceed line 3) (Enter here and on line 3, page 1)			0
6. Balance as of the end of the year (line 3 less line 5)			205,363.49 407

IN UNITED STATES DISTRICT COURT for the northern District, Oklahoma

Plaintiff's Exhibit 10

FORM 1120 L — U.S. LIFE INSURANCE COMPANY INCOME TAX RETURN FOR CALENDAR YEAR 1953 — 1953

U.S. Treasury Department, Internal Revenue Service

PLEASE TYPE OR PRINT PLAINLY

Name: The Atlas Life Insurance Company

Address (number, street, city or town, postal zone number, State): 415 South Boston Avenue, Tulsa 3, Oklahoma

a. Date and place incorporated: September 25, 1918 Oklahoma

b. Employer's identification number: 01-05132

c. Amount of total dividends claimed for current year: 35,485.55

d. Amount of total insurance liabilities as defined in Sec. 801(b)(2): Not applicable to this company

e. Amount of total depreciable assets: 430,508.05

f. Is this a consolidated return? (If "Yes," see instruction 16.) ☐ Yes ☒ No

g. Do you have any variable annuity contracts outstanding? (If "Yes," see section 806 (g).) ☐ Yes ☒ No

h. Are you a mutual or fraternal benefit organization, or an agent directly in the mutual interest of, or in the administration of mutual business? (If "Yes," see section 809.) ☐ Yes ☒ No

i. Did you file Forms 1096 and 1099 for the calendar year in connection with taxable dividends? (See General Instruction 14.) ☒ Yes ☐ No

j. Did you file Forms 1096 and 1099 for the calendar year in connection with other payments? (See General Instruction 14.) ☒ Yes ☐ No

LIFE INSURANCE COMPANY TAXABLE INCOME

1. (a) The taxable investment income (Schedule C)	493	101,043.81		
(b) The gain (loss) from operations (Schedule D)	517	162,057.30	101,043.81	493
(c) The smaller of (a) or (b)			30,506.75	497
2. 50 percent of the excess, if any, of 1(b) over 1(a)			131,550.54	660
3. Life insurance company taxable income (Total lines 1(c) and 2)				

COMPUTATION OF TAX DUE OR REFUND

4. If amount of line 3 is: (a) Not over $25,000— Enter 30 percent of line 3 (22 percent if a consolidated return)				
(b) Over $25,000— Enter $3 percent of line 3 ($4 percent if a consolidated return)	491	68,406.29	62,906.29	491
Subtract $5,500, and enter difference		5,500.00		
5. Less: Credit allowed a domestic corporation for income taxes paid to a foreign country or United States possession (Submit Form 1118)			0	
6. Total income tax (line 4 less line 5)			62,906.29	491
7. Credits for amounts paid on 1953 income tax: (a) Tax paid with application for extension of time in which to file		64,055.79		
(b) Payments and credits on 1953 Declaration of Estimated Tax			64,055.79	
8. If tax (line 6) is larger than payments (line 7), the balance is TAX DUE. Enter such balance here →				
9. If payments (line 7) are larger than tax (line 6) Enter the OVERPAYMENT here →			1,149.50	491
10. Enter amount of line 9 you want: Credited on 1954 estimated tax				
Refunded		1,149.50	491	

SIGNATURE AND VERIFICATION (See Instruction E)

I declare under the penalties of perjury that this return (including any accompanying schedules and statements) has been examined by me, and to the best of my knowledge and belief is a true, correct, and complete return. If the return is prepared by a person other than the taxpayer, his declaration is based on all the information relating to the matter reported in the return of which he has knowledge.

CORPORATE SEAL

(Date) (Signature of officer) (Title)

(Date) (Individual or firm signature) (Address)

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SCHEDULE A.—INVESTMENT YIELD (See Instructions)

Line no.	Gross Investment Income (Section 804(b))	1. Income Received	2. Amount of Dividends	3. Amortization of Premiums	4. Total (Sum of Cols. 1 and 2 less Col. 3)
1.	Interest on:				
	(a) Bonds (except those listed in item 2 below)	36,796.15	1,627.00	785.36	37,637.79
	(b) Bonds (except those listed in item 2 below) which are exempt from tax under section 501(c)	0	0	0	0
	(c) Obligations of States and political subdivisions, the interest on which is excluded from gross income under section 103	0	0	0	0
	(d) Obligations of the United States, its agencies and instrumentalities	46,445.34	22.00	14.00	46,459.34
	(e) Mortgage loans	891,215.68	6,309.98	3,253.05	891,272.61
	(f) Other				975,669.74
	(g) Loans, rents, mortgages, bank deposits, bonds, debentures, etc.	974,457.17	7,961.98	6,749.41	
	Totals				0
2.	Dividends on stock of:				
	(a) Domestic corporations subject to taxation under Chapter 1, I.R.C.				0
	(b) Certain preferred stock of public utilities taxable under Chapter 1, I.R.C.				0
	(c) Foreign corporations				164,995.28
	(d) Other corporations				0
3.	Rents. (Attach schedule)				0
4.	Royalties. (Attach schedule)				0
5.	Leases, investments, etc.				1,140,665.02
6.	Gross income from trade or business other than insurance business. (Attach schedule)				
7.	GROSS INVESTMENT INCOME (Add lines 1-6)				104,602.57
	Deductions (Section 804(c))				121,534.99
8.	Investment expenses. (Attach schedule) (See Schedule H)				19,249.85
9.	Real estate expenses. (Attach schedule)				0
10.	Depreciation. (Attach schedule)				0
11.	Depletion of mines, oil and gas wells, timber, etc. (Attach schedule)				245,387.41
12.	Trade or business deductions as provided in 804(c)(3) (Attach schedule)				895,277.61
13.	Total deductions (lines 8-12)				
14.	INVESTMENT YIELD (See 756 line 1-2)				

SCHEDULE B.—PART I.—POLICY AND OTHER CONTRACT LIABILITY REQUIREMENTS (Sec. 808(a)) (See Instructions)

1.	Adjusted life insurance reserves (from Part V)	22,082,869.23	
2.	Multiplied by the adjusted reserves rate (lesser of lines 1 or 7, Part III)	3.257502%	719,349.91
3.	Interest paid (from Part VI)		44,352.43
4.	Policy and other contract liability requirements (Total of lines 2 and 3)		763,702.34

PART II—ASSETS (Sec. 808(b)(1))

		1. Beginning of Taxable Year	2. End of Taxable Year	3. Mean of column 1 and column 2
1.	Real estate	1,025,738.20	1,042,261.22	1,033,999.71
2.	Mortgages:			
	(a) Without service fees	3,485,485.50	3,376,927.90	3,431,206.70
	(b) With service fees	5,733,561.81	5,599,897.63	5,666,729.72
3.	Collateral loans	275,700.00	272,700.00	274,200.00
4.	Policy loans, including premium notes	2,043,403.98	2,233,301.02	2,138,352.50
5.	Corporate bonds	9,437,901.55	9,659,676.15	9,548,788.85
6.	Stocks	0	0	0
7.	Government obligations, etc. (Submit detailed schedule)	1,733,602.00	2,902,436.00	2,308,019.00
8.	Bank deposits, cash, etc.	987,738.07	1,363,781.39	1,175,760.73
9.	Other assets (Attach schedule)	1,282,546.89	1,213,936.32	1,248,241.61
10.	Totals	25,985,678.00	27,661,919.64	26,823,798.82

*Adjusted under Section 806(a) (Attach schedule)

PART III—EARNINGS RATES (Sec. 808(b))

1.	Current earnings rate (line 14, Schedule A divided by line 10, column 3, Part II)	3.33762
2.	Earnings rate for first preceding year (Attach schedule)	3.31400
3.	Earnings rate for second preceding year (Attach schedule)	3.30410
4.	Earnings rate for third preceding year (Attach schedule)	3.20210
5.	Earnings rate for fourth preceding year (Attach schedule)	3.22957
6.	Total (lines 1-5)	16.38731
7.	Average earnings rate (See instructions)	3.257502%

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PART IV—AVERAGE INTEREST RATE ASSUMED (Sec. 809(a)(2))

1. Nature of Reserve (Life, Annuity, Etc.)	2. Assumed Mortality or Morbidity Table	3. Assumed Interest Rate	4. Method of Computation (Attach Statement and Etc.)	5. Amount of Reserve at Beginning of Taxable Year	6. Amount of Reserve at End of Taxable Year	7. Mean of Columns 5 and 6	8. Interest Required (Multiply Column 7 by Column 3)
1. Life	Various	Various	Various	19,548,850,00	20,786,550,00	20,167,700.00	693,959.35
2. Annuities	Various	Various	Various	893,707.00	924,473.68	909,090.34	25,342.48
3. SCLTC	Various	Various	Various	98,050.28	177,283.43	137,666.86	4,697.52
4. Other	Various	Various	Various	515,154.67	583,134.01	56,144.35	16,876.67
5. Totals						21,761,601.55	740,876.03

6. Average rate of interest assumed in computing life insurance reserves (total of column 8 divided by total of column 7) ..... 3.40420 %

*See instructions for 809(d) and 809(e) adjustments. **Adjusted under 809(e) (Attach schedule)

PART V—ADJUSTED LIFE INSURANCE RESERVES (Sec. 809(a)(1))

1. Mean of the reserves (col. 7, line 5, Part IV)		21,761,601.55
2. (a) Multiplied by that percentage which equals	100%	
(b) Increased by 10 times the average rate of interest assumed (from line 6, Part IV)	34.042 134.04200	
(c) Total	32.57502	
(d) Reduced by 10 times the adjusted reserve rate from line 2, Part I, Schedule B)		101.46698 %
(e) Line (c) less line (d)		22,082,869.23
3. Adjusted life insurance reserves (line 1 multiplied by line 2(e))		0

PART VI—INTEREST PAID (Sec. 805(a))

1. Interest on indebtedness	43,094.36
2. Amounts in the nature of interest	1,258.07
3. Discount on unpaid premiums	44,352.43
4. Total interest paid (lines 1-3)	

SCHEDULE G—BALANCE INVESTMENT INCOME (See Instructions)

1. Policyholders' share (Sec. 809) (line 4, Part I, Sch. B, divided by line 14, Sch. A) but not to exceed 100%	85.30341 %	
2. Company's share	14.69659 %	
3. Total	100 %	

	1. Total	2. Exclusion Policyholders' share (line 1 times col. 1)	3. Company's share (line 1 times col. 1)
4. Interest wholly tax-exempt (line 1(a), column 4, Schedule A)	37,637.79	32,106.32	5,531.47
5. Interest partially tax-exempt (line 1(b) and (c), column 4, Schedule A)	0	0	0
6. (a) Dividends from line 2(a), Schedule A	0	0	0
(b) Dividends from line 2(b), Schedule A	0	0	0
(c) Dividends from line 2(c), Schedule A	0	0	0
(d) Dividends from line 2(d), Schedule A	0	0	0
7. Other items of investment yield (line 14, Schedule A, line 4-6 above)	857,639.82	731,596.01	126,043.81
8. Total (Lines 4-7)	895,277.61	763,702.33	131,575.28
REDUCTIONS			5,531.47
9. Interest wholly tax-exempt (line 4, column 3)			0
10. Interest partially tax-exempt (20/85 of line 5, column 3)			
11. Dividends received deductions			
(a) 85% of dividends from line 6(a), column 3		0	
(b) 82.118% of dividends from line 6(b), column 3		0	
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3		0	
(d) Total, but not to exceed 85% of taxable investment income (line 14, Schedule C) computed without regard to the deduction			0
12. Small business deduction (10% of line 14, Schedule A, not to exceed $25,000)			25,000.00
13. Total (lines 9, 10, 11(d), and 12)			30,531.47
14. Taxable investment income (line 8 less line 13, but not less than zero)			101,043.81

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1. SCHEDULE E—GAIN AND LOSS FROM OPERATIONS (See instructions)			
1. Policyholders' share (See 809 (Line 3, Sch. E-1 divided by line 14, Sch. A), but not to exceed 100%			87.29566 %
2. Company's share			12.70434 %
3. Total			100 %
	1. Total	2. Policyholders' share (Line 1 times col. 1)	3. Company's share (Line 1 times col. 1)
4. Interest wholly tax-exempt (line 1(a), column 4, Schedule A)	37,637.79	32,856.23	4,781.56
5. Interest partially tax-exempt (lines 1(b) and (c), column 4, Schedule A)	0	0	0
6. (a) Dividends from line 2(a), Schedule A	0	0	0
(b) Dividends from line 2(b), Schedule A	0	0	0
(c) Dividends from line 2(c), Schedule A	0	0	0
(d) Dividends from line 2(d), Schedule A	857,619.62	748,664.06	108,955.76
7. Other items of investment yield (line 14, Schedule A less 4-6 above)	895,277.61	781,520.29	113,737.32
8. Total (lines 4-7)			6,168,700.63
9. Gross premiums 6,319,787.11 Less: Return premiums, etc. 151,086.48			0
10. (a) Decrease in reserves (after adjustment under 810(a)) (Attach schedule)			0
(b) Decrease in 810(b)(2) reserves (See line 3, Part IV, Schedule E-2)			582.22
11. Other amounts (Attach schedule)			6,293,029.37
12. Total (lines 8-11)			3,612,468.01
DEDUCTIONS			669,621.65
13. Death benefits, etc.			0
14. Increase in reserves (after reduction for investment yield under 810(b)) (Attach schedule)			4,781.56
15. Assumption by another person of liabilities under insurance, etc., contracts			0
16. Interest wholly tax-exempt (line 4, column 3)			10,183.03
17. Interest partially tax-exempt (30/52 of line 5, column 3)			25,000.00
18. Investment expenses, etc., not deducted on Schedule A (Attach schedule)			170,673.90
19. Small business deduction (10 percent of line 14, Schedule A, not to exceed $25,000)			5,492,728.15
20. Other deductions not deducted on Schedule A (Attach schedule)			
21. Total (lines 13-20)			
22. Dividends received deduction (See instructions)			
(a) 85% of dividends received from line 6(a), column 3	0		
(b) 62.115% of dividends from line 6(b), column 3	0		
(c) 85% of dividends from certain foreign corporations from line 6(c), column 3	0		
(d) Total, but not to exceed 85% of the excess, if any, of line 12 over line 21			0
23. Operations loss deduction (Attach schedule)			0
24. Tentative deduction (lines 21-23)			5,492,728.15
25. Plus: (a) Group life, accident, and health insurance (line 7, Part I, Schedule E-2)			47,749.74
(b) Certain nonparticipating contracts (line 9, Part I, Schedule E-2)			127,116.96
(c) Dividends to policyholders (Line 11, Part I, Schedule E-2)			451,368.22
26. Total deductions (line 24 plus line 25)			6,120,963.07
27. Gain (loss) from operations (line 12 less line 26)			162,057.30

EXHIBIT 1-TE

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SCHEDULE S-1.—REQUIRED INTEREST (Sec. 809(a)(2))

	1. Rate	2. Beginning of Taxable Year	3. End of Taxable Year	4. Mean (Columns 2 plus 3)	5. Column 1 times column 4
1. 810(d)(1) Reserves (From line 5, column 8, Part IV, Schedule B)					740,876.03
2. 810(d)(2) Reserves	Various	730,213.00	705,412.00	717,844.00	21,691.29
3. 810(d)(4) Reserves	Various	490,726.00	534,839.00	512,782.00	17,649.10
4. 810(d)(5) Reserves	Various	50,218.21	62,167.01	56,192.61	1,123.84
5. Required interest (Total, lines 1–4)					781,340.32

SCHEDULE S-2.—PART I—LIMITATION ON LINE 23, SCHEDULE E DEDUCTION (Sec. 809(i))

1. Statutory amount			250 000
2. (a) From line 12, Schedule E	6,283,020.37		
(b) Less: Tentative deduction, line 24, Schedule E	5,492,728.15		
3. Gain from operations (after regard to line 23, Schedule E	790,292.22		
4. Less: Taxable investment income (line 14, Schedule C)	101,043.61		
5. Excess of line 3 over line 4 (but not less than zero)		689,248.61	
6. Maximum possible deduction (or line 23, Schedule E (line 1 plus line 5)		939,248.61	
7. Deduction for group life, accident, and health insurance (Part II) (Not in excess of line 6)		47,749.74	
8. Maximum deduction for certain nonparticipating contracts (line 6 less line 7)		891,498.87	
9. Deduction for certain nonparticipating contracts (Part III) (Not in excess of line 8)		127,116.90	
10. Maximum deduction for dividends to policyholders (line 8 less line 9)		764,381.97	
11. Deduction for dividends to policyholders (Part IV) (Not in excess of line 10)		453,368.22	

PART II—GROUP LIFE, ACCIDENT, AND HEALTH INSURANCE (Sec. 809(d)(8))

1. Net premiums		2,387,487.19
2. Multiplied by		2%
3. Tentative deduction		47,749.74

PART III—CERTAIN NONPARTICIPATING CONTRACTS (Sec. 809(d)(5))

1. (a) Reserves at the end of the taxable year	20,550,115.02		
(b) Reserves at the beginning of the taxable year	19,278,945.38		
(c) Increase (If the difference is negative, enter "0")	1,271,169.64		127,116.96
(d) Multiplied by	10%		
2. (a) Net premiums	3,065,670.34		
(b) Multiplied by	3%		91,970.29
3. Tentative deduction—the greater of line 1 or line 2			127,116.96

PART IV—DIVIDENDS TO POLICYHOLDERS (Sec. 809(d)(3))

1. Dividends paid to policyholders			444,456.63
2. (a) Increased by the excess of (1) over (2):			
(1) Reserves as of the end of the taxable year	204,949.47		
(2) Reserves as of the end of the preceding taxable year	196,037.88		8,911.59
(b) Decreased by the excess of (1) over (2):			
(1) Reserves as of the end of the preceding taxable year			
(2) Reserves as of the end of the taxable year			
3. If positive, enter on line 11, Schedule S-2; if negative, enter on line 10(b), Schedule S			453,368.22

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APPENDIX A

UNITED STATES COURT OF APPEALS
TENTH CIRCUIT

March Term, 1964

No. 7424

ATLAS LIFE INSURANCE COMPANY, APPELLANT

vs.

UNITED STATES OF AMERICA, APPELLEE

APPEAL FROM THE UNITED STATES DISTRICT COURT FOR THE NORTHERN DISTRICT OF OKLAHOMA

May 25, 1964

Before MURRAH, *Chief Judge,* and BREITENSTEIN and HILL, *Circuit Judges*

MURRAH, *Chief Judge.*

The taxpayer, a life insurance company, appeals from a judgment of the District Court (Atlas Life Insurance Co. v. United States of America, 216 F. Supp. 457), denying refund of income taxes paid by it, pursuant to the Life Insurance Company Tax Act of 1959. 26 USC 801 et seq. The Act imposes a tax at ordinary corporate rates upon "life insurance com-

pany taxable income" (§ 802(a)), based upon a three-phase calculation under Section 802(b), which, for our purposes, involves only the first two steps, namely: the determination of "taxable investment income" and "gain from operations" as defined in Sections 804 and 809, respectively.

The taxpayer computed and paid its income taxes for the year 1958 in accordance with the statutory definitions. It thereafter filed claim for refund, contending that the application of the statutory definitions "taxable investment income" and "gain from operations" resulted in the imposition of a tax on tax-exempt interest received from municipal bonds, and that it is therefore entitled to an adjustment under the provisions of Sections 804(a)(6) and 809(b)(4).

The Act of 1959 was promulgated in response to the recognized need for a more permanent and equitable method for determining taxable income of life insurance companies, and was the result of a comprehensive reappraisal of former legislation in the area. The formula for the determination of the tax was conceived in recognition of two salient principles of tax immunity: (1) the policy which has inhered in income tax law since its inception in 1913, to the effect that interest on state securities is excluded from gross income in the computation of the taxpayer's federal tax liability;[1] and (2) in recognition of the traditional concept that a life insurance company should not be taxed on that part of its income which is required to be set aside as a reserve to meet the company's contingent obligations to its policyholders. See 2 USC, Congressional and Administrative News, 86th

[1] This concept is presently embodied as a general rule in Section 103, 26 USC Sec. 103, but is not applicable to the tax treatment of life insurance company tax-exempt interest.

Congress, First Session, 1575; Wurzel, "Tax-Exempt Interest of Life Insurance Companies", 70 Yale L.J. 15 (1960).

The concept of "reserve deduction" is perpetuated in the Act by the division of each and every item of net investment income into two catergories; (1) the policyholders' share which is excluded from tax liability; and (2) the Company's share which is subject to taxation. To effectuate the division of the Company's share from the policyholders' share of the net investment income, the Act first provides for the determination of net investment income, i.e., "investment yield", or gross investment income, including tax-exempt interest, less certain expenses. See §§ 804(c), 804(a)(1) and 809(a)(1). The policyholders' percentage share of investment yield is determined by dividing investment yield into "policy and other contract liability requirements." § 804(a)(1). These requirements are calculated in accordance with the complicated formula provided in Section 805 by adding: the product of the company's "adjusted reserves rate" [2] and its "adjusted life insurance reserves"; [3] the

[2] The "adjusted reserves rate" is the lower of the average earnings rate or the current earnings rate. § 805(b)(1) The "current earnings rate" is the investment yield divided by the mean of the company's assets. § 805(b)(2) The "average earnings rate" is the average of the current earnings rates for the taxable year and for each of the four preceding taxable years. § 805(b)(3).

[3] The "adjusted life insurance reserves" is the mean of life insurance reserves, other than pension plan reserves, adjusted upward by one percent for every tenth of a percent by which the "adjusted reserves rate" is less than the assumed interest rate used in calculating such reserves. If the "adjusted reserves rate" exceeds the assumed interest rate, the reserves are adjusted downward in a similar manner. § 805(c).

pension plan reserves multiplied by the current earnings rate;[4] and interest paid. The percentage derived from the use of this formula[5] represents the policyholders' percentage share, and the remaining portion of 100 percent is the company's percentage share. The life insurance company's percentage share of each and every item of investment yield is then reduced by its percentage share of tax-exempt interest,[6] and the result is taxable investment income.

The second phase for calculating the base tax, i.e., "gain from operations", follows a similar pattern in determining the policyholders' share of investment yield. Though the formula is different,[7] it is sufficient for our purposes to note that, as in phase one, the tax-exempt interest is included to determine the respective percentage shares, and the company's share of exempt interest is then deducted to arrive at gain from operations. See § 809. Thus, after the computation of tax-

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[4] See Footnote 2 for explanation.

[5] It is important to note that investment yield which includes tax-exempt interest is not only the denominator of this formula, but it also significantly affects the determination of the numerator.

i.e. $\frac{\text{policy and other contract liability requirements}}{\text{investment yield}}$

And See Footnotes 2 and 3.

[6] Other deductions are specified in § 804(a)(2)(A).

[7] The policy holders' percentage share of gain from operations is determined by dividing "investment yield" into "required interest" as defined in Section 809(a)(2) instead of "policy and other contract liability requirements." The company's share of each and every item of "investment yield" is then added to the net premium receipts which is reduced by specified deductions, including the company's share of tax-exempt interest. See § 809(d). The result is "gain from operations."

able investment income and gain from operations, Section 802(b) specifies their proper relationship to determine "life insurance company taxable income", i.e., the sum of taxable investment income and 50 percent of the excess of gain from operations over taxable investment income.

The Act then finally provides as an "exception" that "if it is established in any case that the application" of the definitions of taxable investment income and gain from operations "results in the imposition of tax on" any tax-exempt interest, "adjustment shall be made to the extent necessary to prevent such imposition." §§ 804(a)(6) and 809(b)(4).

Making application of the statutory formula in its return for 1958, the taxpayer first computed its tax liability to be $62,615.05. And, it does not now dispute the correctness of the calculations of its tax liability under the formula. The contention is rather that the application of the formula results in its tax liability being increased by $11,252.19, solely because of the receipt of tax-exempt interest and its inclusion in the determination of the tax base. The claim for refund is based on computation of the company's tax liability without the inclusion of tax-exempt interest in investment yield as used in the formula for determining the tax base.

An interpretative analysis of the table below[8] reveals the extent to which the inclusion or exclusion of

[8] This table illustrates the differential in the company's tax liability under the statutory formula and the taxpayer's computations of its liability based upon the exclusion of the tax-exempt interst from investment yield whenever it becomes operative under the formula. Neither party disputes the correctness of the arithmetic computations which reflect the

tax-exempt interest in or from investment yield permeates the whole computation of tax liability. Thus, in phase one, a reduction of the adjusted reserves rate results because it is the lower of the two earnings rates, which are in essence determined by dividing assets into investment yield. See Footnote 2. The effect of the reduction in the adjusted reserves rate on policy and other contract liability requirements is par-

application of their respective theories of the company's statutory tax liability.

Phase 1: Computation of Taxable Investment Income

Item	Statutory formula	Exempt interest excluded
Investment Yield	$894, 277. 61	$857, 639. 82
Current Earnings Rate	3. 33390%	3. 19731%
Average Earnings Rate	3. 253782%	3. 12297%
Adjusted Reserve Rate	3. 253782%	3. 13397%
Adjusted Life Ins. Reserves Rate	$22, 090, 965. 28	$22, 375, 659. 00
Policy & Other Contract Liability Requirements	$763, 144. 28	$743, 137. 55
Policyholders' Percentage Share	85. 3364%	86. 6491%
Company's Percentage Share	14. 6636%	13. 3509%
Company's Share of Items of Investment Yield	$131, 183. 29	$114, 502. 27
Deduction of Tax-Exempt Interest	$5, 372. 42	none
Taxable Investment Income	$100, 760. 87	89, 502. 27

Phase 2: Computation of Gain from Operations

Item	Statutory formula	Exempt interest excluded
Investment Yield	$894, 277. 61	$857, 639. 82
Required Interest	781, 540. 32	781. 540. 32
Policyholders' Percentage Shares	87. 3934%	91. 1269%
Company's Percentage Share	12. 60652%	8. 8731%
Company's Share of Items of Investment Yield	$112, 737. 29	$76, 099.50
Deduction of Tax-Exempt Interest	$4, 618. 75	none
Gain from Operations	$161, 220. 08	$129, 201. 04

Tax Computation

Item	Statutory formula	Exempt interest excluded
Taxable Investment Income	$100, 760. 87	$89, 502. 27
50% of the Excess of Gain from Operations over Taxable Investment Income	30, 229. 61	$19, 849. 39
Life Insurance Co. Taxable Income	$130, 990. 48	$109, 351. 66
Total Income Tax*	$62, 615. 05	51, 362. 86

*The $11,252.19 differential constitutes the claimed refund.

tially offset by the increase in the adjusted life insurance reserves caused by the greater difference between the adjusted reserves rate and the assumed interest rate. See Footnote 3. Although policy and other contract liability requirements are lower, the policyholders' percentage share is greater because of the exclusion of the exempt interest from investment yield. Conversely, the Company's percentage share is greater because of the inclusion of exempt interest in investment yield. Thus, the percentage differential and the ultimate increase of taxable items of investment yield included in taxable investment income are attributable to the inclusion of tax-exempt interest.

Similarly, in the phase two computation, exclusion of tax-exempt interest from investment yield results in an increased policyholders' percentage share, because it is calculated by dividing investment yield into required interest which remains the same. Thus, the difference in the Company's percentage shares is attributable to the inclusion of the exempt interest, and this in turn accounts for the variation in gain from operations.

The trial court's conclusion that the receipt by the taxpayer of exempt interest was not in fact taxed, is apparently based upon the interpretation of the statutory formula, to the effect that the "company's tax-exempt interest is included in gross income and then deducted before reaching the tax base of the Taxpayer." Atlas Life Insurance Co. v. United States of America, supra, p. 460. The fallacy of this interpretation is that it fails to recognize what the Government seems to concede, that the increase in the Company's share of investment yield by the inclusion of exempt interest in the formula for determining the respective percentage shares is not offset by the deduction of the Company's percentage share of exempt

interest, and that the ultimate tax liability is in fact increased.

The judgment of the trial court is sought to be sustained on the theory that although the inclusion of tax-exempt interest in the formula results in an increase in the Company's share of all other income, it will be exactly what it would have been if the Company had received taxable income, and that the application of the statutory definitions does not therefore result in a tax on tax-exempt interest. The Government says this is "precisely what Congress intended." And, they justify it by emphasizing the design of the statute to divide the ownership of all investment income, and that this has the concomitant effect of dividing the tax-exempt interest between the policyholders and the Company. This method of prorating the exempt interest is said to be an exertion of the "full power" of Congress to classify income for tax purposes, and in this particular case, to prevent a double deduction through the interplay of the exclusion of the policyholders' share and the deduction of exempt interest.

The Government attacks the taxpayer's formula which eliminates the exempt interest from the computation as in effect allocating all taxable dollars to the policyholders and all tax-exempt dollars to the Company, thus creating a loophole which the statute was designed to prevent.

If, as the Government contends, the Congress, in enacting the taxing formula, intended to test anew the doctrine of inter-governmental tax immunity by exerting its full constitutional powers to classify income for tax purposes, our inquiry is simply whether, judged by present-day concepts, the Congress overstepped its constitutional bounds. But, the taxpayer takes the position that Congress legislated with an

eye to the doctrine of National Life Insurance Co. v. United States, 277 U.S. 503; and Missouri v. Gehner, 231 U.S. 313, according to which the sovereign may not subject a taxpayer to a greater burden on his income solely because of the receipt of tax-exempt interest. As we view our lawsuit in the context of the respective contentions of the parties, it involves the determination of the extent to which the Congress intended to exercise its power of taxation with respect to tax-exempt interest received by life insurance companies.

While resort to legislative history is usually justified only in cases of ambiguity in the statutory language, i.e., see Nicholas v. Denver & R.G.W. R. Co., 195 F. 2d 428, it is frequently relied upon for the ascertainment of a Congressional purpose as embodied in the final enactment. See Flora v. United States, 362 U.S. 145; United States v. Harriss, 347 U.S. 612; United States v. American Trucking Assn., 310 U.S. 534; Caminetti v. United States, 242 U.S. 470; Sutherland on Statutory Construction, Vol. 2, p. 481 et seq. In the words of Mr. Justice Frankfurter, dissenting in Reed v. Pennsylvania RR Co., 351 U.S. 502, 510, "The process of judicial construction must be mindful of the history of the legislation, of the purpose which infused it, of the difficulties which were encountered in effectuating this purpose, of the aims of those most active in relieving these difficuties." To support their positions, both the Government and the taxpayer rely heavily on the extensive legislative history of the Act as influenced by the contemporary case law. We will therefore examine it to determine the purpose and scope of the taxing act.

The parties start with the Revenue Act of 1921 and particularly Section 245(a), 42 Stat. 227, 261, which provided that in the case of life insurance companies,

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net income means gross income less certain deductions, inter alia, (1) the amount of interest received from tax-exempt securities; and (2) a reserve deduction reduced by the amount of exempt interest. In National Life Insurance Co. v. United States, supra, the Supreme Court held that the diminution of the reserve deduction by the amount of exempt interest had the effect of destroying the guaranteed exemption. The underlying principle, as announced by the Court, was to the effect that a taxpayer may not be subject to a greater tax burden on his taxable income solely by reason of the receipt of tax-exempt interest.

There were strong and persuasive dissents in which it was suggested that since the reserve deduction was a matter of grace or bounty, the Congress was perfectly free to reduce it by the amount of exempt interest, or any other amount for that matter. The dissenters did not think that the Constitution or the laws guaranteed that "a holder of tax-exempt bonds, shall be better off than if he held only taxable securities"; nor did it require that "those who do not hold tax-exempt securities shall, in respect to every tax, be subjected to a heavier burden than the owners of tax-exempt bonds." National Life, supra, p. 528.

Apparently, on the authority of National Life, the Supreme Court in Missouri v. Gehner, supra, reversed the Missouri Supreme Court which, in considering a state property tax, had upheld the apportionment of reserves and claims between taxable and non-taxable assets, including United States bonds. The Court restated the National Life doctrine to the effect that a "State may not subject one to a greater burden on his taxable property merely because he owns a tax-exempt government securities." Missouri v. Gehner, supra, p. 321. The same dissenters, speaking through Mr. Justice Stone in Gehner, were of the opinion that

nothing in National Life required a reversal of this case. They insisted that tax-free securities might well be realistically held accountable for their share of reserves for claims in computing the tax. Otherwise, said they, an affirmative benefit is conferred upon the ownership of tax-exempt securities "at the expense of the taxing powers of the state, by relieving the owner from the full burden of taxation on net worth to which his taxable assets have in some measure contributed." Gehner, supra, p. 328. It would thus appear that the dissenters would have given little or no respect to the doctrine of intergovernmental tax immunity. In any event, it seems reasonable to say that the same vigorous dissenters in both National Life and Gehner would find no fault in the asserted power to apportion tax-exempt income between the reserve deduction and taxable income for the purpose of arriving at the taxpayer's tax liability.

Another contemporary decision of the Supreme Court, Denman v. Slayton, 282 U.S. 514, also involved the 1921 taxing Act, particularly Section 214(a)(2), 42 Stat. 227, 239, which denied a deduction for interest paid on indebtedness incurred to purchase or carry tax-exempt securities. In his return for the taxable year 1922, the taxpayer excluded interest received on tax-exempt muncipal bonds and deducted the interest on money borrowed to purchase and carry the bonds. The Commissioner disallowed the deduction and the lower court sustained the taxpayer on the authority of National Life. But, a unanimous Supreme Court, in an opinion by the writer of National Life, held that National Life was "radically different", and that its doctrine did not control. The Court went on to say that "while guaranteed exemptions must be strictly observed, this obligation is not inconsistent with reasonable classification designed to subject all to the

payment of his just share of a burden fairly imposed." Denman v. Slayton, supra, p. 519.

Such was the state of the decisional law as Congress continued to wrestle with the problem of finding a just and appropriate method of determining life insurance companies' taxable income. The 1921 Act apparently was not amended to reflect the National Life restriction on reserve deduction until the 1932 Act, which simply deleted the objectional provision for diminution of the reserve deduction by the amount of exempt interest. 47 Stat. 169, 224; § 203 of Revenue Act of 1932. This text of the law was carried forward and observed until 1942 when a new system was introduced. 56 Stat. 798, 868–870, §§ 202 and 203 of the Revenue Act of 1942. This Act prescribed a reserve deduction expressed as a percentage of investment income, including tax-exempt interest based on industry-wide experience. Each company applied this percentage to its net investment income, but was allowed to deduct all its tax-exempt interest before prorating its net investment income.

As in our formula, the 1942 Act included exempt interest in its formula for determining the industry-wide reserve deduction percentage. And, this percentage, which was applied to determine the individual company reserve deduction, was decreased by the inclusion of tax-exempt interest. This had the theoretical effect of increasing the percentage of net investment income which is taxable. But no taxpayer was induced to test the added tax burden as against the doctrine of National Life, apparently for two reasons: (1) the industry-wide reserve deduction percentage was so great that the individual company's net taxable investment income was minuscule; (2) each company could minimize its tax burden by purchasing tax-exempt securities because the income

therefrom was not included in the computation of their individual tax liability. This situation obtained without significant change until 1958. See Wurzel, Yale L.J., supra, p. 20–21.

After considerable study, the House passed a Bill which provided for the determination of insurance company tax liability in three steps on an individual company basis. The step one base was the difference between the taxable net investment income, as reduced by the total amount of exempt interest, and the reserve deduction, as reduced by its allocable share of exempt interest. See: §§ 804 and 805, H.R. 4245, Hearings Before Senate Finance Committee on H.R. 4245, 86th Cong., First Sess. (1959), pp. 4–7. The provisions of the House Bill in this regard are noticeably similar to the so-called "Add-Back" provisions of Section 245(a)(2) of the 1921 Act, the distinction being that the reserve deduction was not diminished by the total amount of exempt interest, but only its prorata share. It is also noteworthy that the mathematical result of the House formula is conceded by all parties to be identical with the result obtained in the final Act.[9] The insurance companies apparently did not detect the shades of the 1921 Act in the House Bill until it came before the Senate. It was then that they apparently became aware that their tax liability might be increased solely by reason of the receipt of tax-exempt interest.

When the Treasury came before the Senate Finance Committee to urge the adoption of the House Bill, the Treasury witness, explaining the provisions of the proposed legislation, observed that while the tax-exempt interest was excluded in both phases of the

[9] The formula for step 2 proceeded along the same lines and, with a result also identical to the final Act. See: § 809, H.R. 4245, Hearings, supra, pp. 8–10.

Bill, an adjustment was made "to the deductions to avoid a double benefit * * *." He also agreed that it was "probably a fair statement" to say that the adjustment was in reality charging a part of the operating expense against tax-free interest. When asked why the Treasury proposed to tax-exempt interest, "even partially", the witness candidly answered: "Because we think it is right." In answer to further queries whether such a provision would render the bill unconstitutional, the witness also candidly admitted that he thought the question "might very well be litigated", and that "we should determine with the best advice we can, as to whether or not we today think such a provision is unconstitutional, and if we believe it is not, and if we believe the provision is right, we ought to include it in the bill." Hearings, supra, pp. 43–44.

The extensive pro and con hearings before the Senate Finance Committee on the House Bill reflect strong representations on the part of insurance companies and those interested in the marketability of tax-exempt securities, to the effect that the proration of the tax-exempt interest between the reserve deduction and net investment income resulted in a tax burden on exempt interest, contrary to National Life, and was therefore constitutionally impermissible. In short, they rested their case principally on the constitutional limitations of National Life and Gehner.[10] There was the further strong representa-

[10] One witness, president of a large life insurance company, in his statement purported to represent 120 companies: "We believe that, in its treatment of tax-exempt interest, H.R. 4245 contravenes the decision of the Supreme Court in the case of National Life v. United States. We think that if it was unconstitutional to add back 100 percent of tax-free interest to the tax base under the 1921 law, then adding back only 70

tions that the resultant burden on the exempt security would adversely affect their marketability in competition with taxable securities—a result which Congress would wish to avoid."[11]

As we summarize the Government's representations to the Senate Committee, they were based primarily on the thesis that the trend of the recent Supreme Court decisions was away from the National Life doctrine of intergovernmental tax immunity, and toward the minority view; that in any event, the House Bill formula was unlike the 1921 formula, and in substance the same as the 1942 formula, which

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percent of such interest is unconstitutional, too." Hearings, supra, p. 305. He also filed a lawyer's brief on the constitutional question. See Hearings, p. 308.

Another witness, vice-president of a life insurance company, stated that "As H.R. 4245 now stands, it is not possible for a life insurance company to invest either its capital or surplus funds in municipal bonds and receive the interest on them free from tax; at least, not unless it first invests all of its policyholders' reserve funds in municipal bonds. And this would be absurd." Hearings, supra, p. 406. He too supplemented his testimony with a memorandum on the constitutionality of taxation of tax-exempt interest, in which it was "observed that the pro rata disallowance rule under the Ohio (sic) statute which was held unconstitutional in the Missouri v. Gehner case is very similar to the pro rata rule contained in Section 809(d) of the present bill." Hearings, supra, 408.

See also: Hearings, supra, pp. 614, 632.

[11] The executive director of an association representing 13,000 municipal governments submitted a statement in which H.R. 4245 was characterized as "* * * the opening wedge to apply the same principal to all other taxpayers." It also noted the "* * * * higher interest rates which State and local governments would have to pay if such a Federal tax were imposed on all their bonds in the future." Hearings, supra, p. 699. An association composed of 6,000 county officials endorsed this statement. See Hearings, supra, p. 699–700.

See also Id., p. 106, 187–188, 252, 305, 405, 632, 687.

had the effect of preventing a double deduction for tax-exempt interest, and which had never been challenged in the courts. See: Hearings, supra, p. 48–51.

It is not manifestly clear what considerations prompted the Senate Committee to revise the House Bill, but the fact is that it did reapproach the problem somewhat differently with respect to the treatment of tax-exempt interest. One of the innovations deemed important in the Senate version was division of the ownership of income and expense items between the policyholders and the insurance company, with only the company's share being taken into account for tax purposes. See: 2 USC Cong. & Adm. News, supra, p. 1580. The Senate Committee seemed to think that by dividing ownership of investment income by the use of a formula which included all tax-exempt interest, and the deduction of the company's pro rata share from its tax base, was preferable to the House formula, which excluded all tax-exempt interest from investment income, but reduced the deduction for policy and other contract liability requirements by its pro rata share of exempt interest.[12] Apparently, being unsure of the tax consequences of what they had done, but "to give further assurance that no tax is to be imposed on tax-exempt interest", the Senate then added the exception Sections

[12] After comparing the two treatments, the Committee Report added: "Your committee believes that the division of income and expense items between the policyholders and the insurance company, with only the latter being taken into account for tax purposes, is a much better concept to follow. It also makes it clear that items which are properly exempt * * * such as tax-exempt state and municipal bond interest * * * are properly divided between the policyholders and the life insurance company and that as far as the latter is concerned, namely, the only portion included in the tax base, full allowance is made for these items.". 2 USC Cong. & Adm. News, p. 1580.

804(a)(6) and 809(b)(4). 2 USC Cong. & Adm. News, supra, p. 1592.

When the Senate version came to the Floor for consideration the Chairman of the Finance Committee, reporting on the Bill, stated that it was "the intention of the Committee not to impose any tax on tax-exempt interest"; and that the "Treasury has assured the Committee that this formula does not impose any tax on tax-exempt interest. The bill adds a proviso to the effect that if the formula I have described does not result in the imposition of tax on this item, the formula is to be adjusted so that it does not do so." [13]

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[13] Senator Curtis, who was asked to make the detailed explanation of the statute, made the following statement on the floor of the Senate before the amended version was adopted: "I wish to mention a matter which has deeply concerned your committee. That was the problem of making sure that we did not, by inadvertence, tax any of a life insurance company's tax-exempt interest income. The bill meets this problem most accurately and fairly." He concluded his discussion of the treatment of tax-exempt interest with the following example: "Under the bill, $70 of the $100 tax-exempt interest income would be allocated to policyholders' reserve, and the other $30 would be allocated to the company. Since no part of the policyholders' reserves would become a part of the tax base, no part of the $70 tax-exempt interest allocated to those reserves would be taxed. Moreover, no part of the $30 allocated to the company would be taxed, because a deduction of the full $30 would be made in determining what part of the company's share of its investment income was to be subject to tax.

"Thus, no tax-exempt income or credits of life insurance companies will be included in the tax base of such companies, under this bill. This should allay any fear that any constitutional provision is transgressed." 105 Cong. Record, Part 6, p. 8429. Representative Mills, after the conference committee reached agreement on the final Act, reported to the House: "It is my belief that the appropriate deduction was allowed by the House bill and that these provisions of the final bill, which closely follow the Senate amendments, make no change of sub-

105 Cong. Record, Part 6, p. 8401. A letter from the Treasury, read to the Senate, stated that "It has been the objective of the provisions in question to exclude fully from tax in the hands of life insurance companies the interest on State and municipal bonds. At the same time, however, it has been considered essential not to allow anything in the nature of a double deduction or tax loophole arising from the special characteristics of the unique formula to be applied to these companies." The letter again reviewed the statutory formula for determining an insurance company's taxable income and, referring to the exception sections, expressed the view that "this additional language is not necessary, since we cannot envision a situation in which the operation of the proposed tax formula would result in the substantive imposition of tax on municipal bond interest or on any other form of tax-exempt income." 105 Cong. Record, Part 6, p. 8402. What the Treasury meant by a "substantive imposition" of tax on exempt interest is a matter of doubt and speculation. But, considered in the context of the views expressed before the Committee, and the position taken here, it seems fair to assume that the Treasury recognized that though the inclusion of tax-exempt interest in the formula resulted in an increase of the taxpayer's burden, it was nevertheless within the taxing power of the Congress and would not therefore result in an impermissible imposition, and we consequently have no need to employ the exception provisions of the statute.

Whatever may be said of the extent of the Congressional power to indirectly burden exempt interest in

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stance." 105 Cong. Record, Part 8, p. 10412. He further stated that the final Act "* * * clarified the language of the House bill to make it definite that we do not intend to tax the interest on tax-exempt securities." Id., 10414.

the exercise of its power to classify all income for purposes of taxation; and whatever may be said of the government's conception of the Congressional intent and purpose to observe those precepts in the enactment of this legislation, it seems manifestly plain to us that Congress did not intend to invade the integrity of the intergovernmental tax immunity doctrine as exemplied in the decisional law when the legislation was under consideration. The prenatal history of this Act convinces us that Congress legislated with an ear to the problem of the marketability of state and municipal securities, and with an eye to the constitutional limitations of National Life on the Congressional power to increase the tax burden of a life insurance company, solely by reason of the receipt of interest from state or municipal securities.

The question then is whether this is a National Life-Gehner case. The trial court did not think so, and, basing its decision on Slayton, concluded that there was in fact no imposition of a prohibited tax. We conclude that our case is within the ambit of the National Life case, which is "radically different" from Slayton. In National Life, the Court invalidated Section 245(a) of the 1921 Act because it in effect increased the taxpayer's tax liability, solely by reason of the receipt of tax-exempt interest. In Slayton, the same Court upheld Section 214(a) of the same Act as a valid measure to prevent the avoidance of tax on taxable income by the simple expedient of borrowing to purchase tax-exempt securities. As the Court observed in Slayton, the taxpayer "was not in effect required to pay more upon his taxable receipts than was demanded of others who enjoyed like incomes solely because he was the recipient of interest from tax-free securities—a result which we found would have followed enforcement of the literal provisions of Section 245(a)." Denman v. Slayton, supra, 519.

And see Helvering v. Independent Life Insurance Co., 292 U.S. 371, 381.

While the extent of the burden on the exempt interest and the form and method of imposing it in our case may differ from National Life, the taxable effect differs only in degree. In both instances the liability of the taxpayer is increased, solely by reason of the receipt of tax-exempt interest, and no form or method for determining it can disguise its incidence. We conclude that the application of the definitions in the Act does result in the imposition of a tax on exempt interest, and the taxpayer is therefore entitled to an adjustment to the extent necessary to prevent such imposition.

It is incumbent upon the taxpayer to prove the amount of the adjustment. It says that it is $11,252.19, and arrives at this amount by simply eliminating exempt interest wherever it is operative in the computation under the statutory formula. While the Government does not quarrel with the taxpayer's arithmetic, it strenuously denies support or sanction of the formula by which it is computed. In that respect it says that the treatment of the tax-exempt interest is the same as if the money used to purchase tax-exempt securities had remained idle.

Be that as it may, the Congress has expressly provided for an adjustment to the extent necessary to prevent the imposition of tax on the exempt interest. And, since we hold that the application of the statutory definitions does in fact result in a prohibited imposition; and since the taxpayer's computations are based upon the elimination of that interest, we must conclude that the adjustment does no more than prevent the prohibited imposition.

Insofar as the judgment of the trial court denies refund of $11,252.19, it is reversed with directions to enter judgment accordingly.

BREITENSTEIN, *Circuit Judge* (concurring in result).

I find it unnecessary to go into the details of the mathematical formulas provided by §§ 804 and 809 of the Life Insurance Company Income Tax Act of 1959, 26 U.S.C. §§ 801–820, or to explore the legislative history of that Act.

Income of the companies subject to the Act is divided into a policyholders' share and a company's share. The company is taxed on its share. The uncontroverted showing of Atlas is that, on the facts pertaining to its 1958 income, the inclusion of interest on tax-exempt securities in the statutory formulas increases the company's share and results in a tax of $11,252.19 more than would have been payable if tax-exempt income had been excluded therefrom. The imposition of tax in this amount results solely from the inclusion in the formulas of income from tax-exempt securities.

Both § 804(a)(6), relating to taxable investment income, and § 809(b)(4), relating to gain from operations, provide that if the application of the definitions found in those sections results in the imposition of a tax on interest which under § 103 is excluded from gross income (interest on state, municipal, and certain other securities), "adjustment shall be made to the extent necessary to prevent such imposition."

The operation of the formulas is such that the tax actually is imposed on taxable income, but this result does not excuse the United States for failing to make the adjustment. National Life Insurance Company v. United States, 277 U.S. 508, and Missouri ex rel. Missouri Insurance Company v. Gehner, 281 U.S. 313, hold that a tax is imposed on tax-exempt property by an increase in tax on taxable property arising solely from the ownership of tax-exempt property.

I grant the power of Congress to classify income, within constitutional limits, for income tax purposes;

and I recognize that the reserve deduction which comes from the division of income into the noted shares is a matter of congressional grace or bounty. The issue is the exercise of a power rather than the existence of a power. The statute under consideration discloses a clear intent not to tax income from state and municipal securities. No uncertainty in this regard exists to require recourse to legislative history for the ascertainment of congressional intent.

We are bound by the National Life and Missouri v. Gehner decisions. With full knowledge of those decisions, Congress provided that if the application of the statutory method causes a tax on tax-exempt income an adjustment shall be made to prevent such a result. By refusing to make the necessary adjustment the government, in effect, has written §§ 804(a)(6) and 809(b)(4) out of the statute. Atlas is entitled to recover the overpayment.

JUDGMENT

First Day, May Term, Monday, May 25th, 1964

Before Honorable ALFRED P. MURRAH, *Chief Judge*, and Honorable JEAN S. BREITENSTEIN and Honorable DELMAS C. HILL, *Circuit Judges*

This cause came on to be heard on the transcript of the record from the United States District Court for the Northern District of Oklahoma and was argued by counsel.

On consideration whereof, it is ordered and adjudged by this court that insofar as the judgment of the trial court denies refund of $11,252.19, it is reversed with directions to enter judgment accordingly.

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Supreme Court of the United States

No. ---------- , October Term, 19 64

UNITED STATES OF AMERICA,

Petitioner

VS.

ATLAS LIFE INSURANCE COMPANY

ORDER EXTENDING TIME TO FILE PETITION FOR WRIT OF CERTIORARI

UPON CONSIDERATION of the application of counsel for petitioner(s),

IT IS ORDERED that the time for filing petition for writ of certiorari in the above-entitled cause be, and the same is hereby, extended to and including September 11, 19 64.

Associate Justice of the Supreme Court of the United States.

Supreme Court of the United States

No: 489 ----- , October Term, 19 64

United States,

Petitioner,

v.

Atlas Life Insurance Company

ORDER ALLOWING CERTIORARI. Filed December 7 ------ , 19 64.

The petition herein for a writ of certiorari to the United States Court of Appeals for the Tenth ---------- Circuit is granted, and the case is placed on the summary calendar.

And it is further ordered that the duly certified copy of the transcript of the proceedings below which accompanied the petition shall be treated as though filed in response to such writ.